











# ANNUAL REPORT

of the Secretary of the Treasury  
on the State of the Finances



*FISCAL YEAR 1980*



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# ANNUAL REPORT

of the Secretary of the Treasury  
on the State of the Finances



*FISCAL YEAR 1980*

DEPARTMENT OF THE TREASURY

*DOCUMENT NO. 3282*

*Secretary*



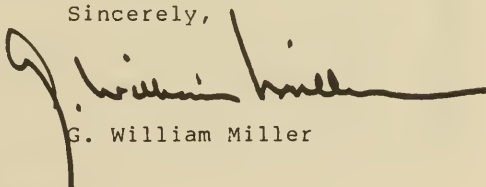
THE SECRETARY OF THE TREASURY  
WASHINGTON

January 15, 1981

Dear Sirs:

I have the honor to submit to you  
a report on the state of the finances  
of the United States Government for the  
fiscal year ended September 30, 1980.  
This submission is in accordance with  
31 U.S.C. 1027.

Sincerely,



G. William Miller

President of the Senate  
Speaker of the House of Representatives





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Term of service		Officials
From	To	
Jan. 23, 1977	Aug. 4, 1979	<b>Secretaries of the Treasury:</b>
Aug. 7, 1979	.....	W. Michael Blumenthal, Michigan.
		G. William Miller, California.
Mar. 3, 1976	Jan. 23, 1977	<b>Deputy Secretaries:</b>
May 3, 1977	.....	George H. Dixon, Minnesota.
		Robert Carswell, New York.
Mar. 30, 1977	Feb. 23, 1980	<b>Under Secretary for Monetary Affairs:</b>
		Anthony M. Solomon, Virginia.
Mar. 30, 1977	.....	<b>Under Secretary (Counselor):</b>
		Bette B. Anderson, Georgia.
Aug. 4, 1977	Aug. 29, 1980	<b>General Counsel:</b>
		Robert H. Mundheim, Pennsylvania.
Apr. 11, 1972	Apr. 28, 1977	<b>Assistant Secretaries:</b>
Feb. 28, 1977	Dec. 7, 1977	Warren F. Brecht, Connecticut.
Mar. 30, 1977	.....	Laurence N. Woodworth, Maryland.
Mar. 31, 1977	.....	Gene E. Godley, District of Columbia. <sup>2</sup>
Apr. 29, 1977	.....	C. Fred Bergsten, New York. <sup>2</sup>
Apr. 29, 1977	Nov. 15, 1978	Roger C. Altman, New York.
Apr. 29, 1977	.....	William J. Beckham, Jr., Michigan.
May 16, 1977	Sept. 30, 1979	Joseph Laitin, Maryland.
Jan. 30, 1978	.....	Daniel H. Brill, Maryland.
June 26, 1978	.....	Richard J. Davis, New York.
July 3, 1979	.....	Donald C. Lubick, Maryland.
Apr. 4, 1980	.....	W. J. McDonald, District of Columbia.
		Curtis A. Hessler, District of Columbia.
July 29, 1975	Dec. 31, 1977	<b>Fiscal Assistant Secretaries:</b>
July 5, 1978	.....	David Mosso, Virginia.
		Paul H. Taylor, Maryland.
Aug. 3, 1977	.....	<b>Treasurer of the United States:</b>
		Azie T. Morton, Virginia.

<sup>1</sup> For officials from Sept. 11, 1989, to Jan. 20, 1977, see exhibit 62, 1977 Annual Report.

<sup>2</sup> Act of May 18, 1972, provided for two Deputy Under Secretaries, to be designated Assistant Secretaries by the President as desired.

# **PRINCIPAL ADMINISTRATIVE AND STAFF OFFICERS OF THE DEPARTMENT OF THE TREASURY AS OF SEPTEMBER 30, 1980**

Secretary of the Treasury .....	G. William Miller
Deputy Secretary of the Treasury .....	Robert Carswell
Under Secretary for Monetary Affairs .....	(Vacancy)
Under Secretary .....	Bette B. Anderson
General Counsel .....	David R. Brennan (acting)

## Office, Secretary of the Treasury:

Executive Assistant to the Secretary .....	Randall K. C. Kau
Special Assistant to the Secretary .....	Jeffrey J. Rosen
Confidential Assistant to the Secretary .....	Lisa Astudillo

## Office, Deputy Secretary of the Treasury:

Inspector General .....	Leon Wigrizer
Director, Office of Audit .....	Eugene H. Essner
Executive Assistant to the Deputy Secretary ...	William A. Anawaty
Executive Secretary .....	Steven L. Skancke (acting)
Deputy Executive Secretary .....	Steven L. Skancke
Special Assistant to the Secretary (National Security) .....	J. Foster Collins
Special Assistant to the Secretary (Consumer Affairs) .....	Sally Vogel
Director of Small and Disadvantaged Business Utilization .....	Linda L. Coffin

## Office, Under Secretary for Monetary Affairs:

Assistant Secretary (International Affairs) .....	C. Fred Bergsten
Deputy Assistant Secretary (Trade and Investment Policy) .....	Robert Cornell
Deputy Assistant Secretary (Commodities and Natural Resources) .....	Charles Schotta
Deputy Assistant Secretary (International Monetary Affairs) .....	Thomas B. Leddy
Deputy Assistant Secretary (Developing Nations) .....	Arnold Nachmanoff
Deputy Assistant Secretary (International Economic Analysis) .....	John R. Karlik
Deputy to the Assistant Secretary (Saudi Arabian Affairs) .....	(Vacancy)
Deputy to the Assistant Secretary and Secretary of IMG (International Monetary Group) .....	(Vacancy)
Inspector General .....	(Vacancy)
Fiscal Assistant Secretary .....	Paul H. Taylor
Deputy Fiscal Assistant Secretary .....	Gerald Murphy
Assistant Fiscal Assistant Secretary (Banking) .....	John A. Kilcoyne
Assistant Fiscal Assistant Secretary (Financing) .....	Philip J. Fitzpatrick

## Office, Under Secretary:

Special Assistant to the Under Secretary ..	Faye P. Hewlett
Special Projects Officer .....	Felix S. Williams

Assistant Secretary (Administration) .....	W. J. McDonald
Deputy Assistant Secretary (Administration) .....	Martha A. Thompson
Director, Office of Administrative Programs .....	Edward W. Brooks
Director, Office of Budget and Program Analysis .....	Arthur D. Kallen
Director, Office of Computer Science .....	James F. Kerrigan (acting)
Director, Office of Equal Opportunity Program .....	(Vacancy)
Director, Office of Management and Organization .....	William J. Rhodes
Director, Office of Personnel .....	Henry C. DeSeguirant
Director, Office of Procurement .....	Thomas P. O'Malley
Assistant Secretary (Enforcement and Operations) .....	Richard J. Davis
Deputy Assistant Secretary (Operations) .....	John P. Simpson
Deputy (Regulatory and Trade Affairs) .....	(Vacancy)
Director, Office of Operations .....	John W. Mangels
Deputy Assistant Secretary (Enforcement) .....	William W. Nickerson
Director, Foreign Assets Control .....	Dennis O'Connell
Special Assistant to the Assistant Secretary (Enforcement and Operations) .....	Catherine H. Milton
Treasurer of the United States .....	Azie T. Morton
Assistant to the Treasurer of the United States .....	Darryl H. Fagin
Office, General Counsel:	
Deputy General Counsel .....	David R. Brennan
Assistant General Counsel and Chief Counsel, Internal Revenue Service .....	N. Jerold Cohen
Assistant General Counsel .....	Arnold Intrater
Assistant General Counsel .....	Russell L. Munk
Assistant General Counsel .....	Jordan A. Luke
Assistant General Counsel .....	Luke D. Lynch
Counselor to the General Counsel .....	Wolf Haber
Director of Practice .....	Leslie S. Shapiro
Assistant Secretary (Tax Policy) .....	Donald C. Lubick
Deputy Assistant Secretary (Tax Legislation) .....	Daniel I. Halperin
Deputy Assistant Secretary (Tax Analysis) .....	Emil M. Sunley
Director, Office of Tax Analysis .....	Harvey Galper
Tax Legislative Counsel .....	John M. Samuels
International Tax Counsel .....	H. David Rosenbloom
Director, Office of Industrial Economics .....	(Vacancy)
Assistant Secretary (Legislative Affairs) .....	Gene E. Godley
Deputy Assistant Secretary (Legislative Affairs) .....	(Vacancy)
Deputy Assistant Secretary (Legislative Affairs) .....	Robert E. Moss
Special Assistant to Assistant Secretary .....	Geoffrey G. Peterson
Special Assistant to Assistant Secretary .....	E. Douglas Frost
Special Assistant to Assistant Secretary .....	Donald F. Terry
Assistant Secretary (Economic Policy) .....	Curtis A. Hessler
Special Assistant to Assistant Secretary (Economic Policy) .....	Roger H. Bezdek
Deputy Assistant Secretary (Economic Policy) .....	Richard F. Syron
Director, Office of Financial Analysis .....	John H. Auten
Director, Office of Special Studies .....	Maynard S. Comiez
Assistant Secretary (Domestic Finance) .....	Roger C. Altman
Deputy Assistant Secretary (Financial Institutions and Capital Markets Policy) .....	John J. Mingo

Director, Office of Securities Markets Policy .....	Philip C. Loomis
Director, Office of Capital Markets Legislation .....	Gordon Eastburn
Deputy Assistant Secretary (Corporate Finance)	Brian M. Freeman
Deputy Assistant Secretary (State and Local Finance) .....	Robert W. Rafuse, Jr.
Director, Office of New York Finance ....	John J. McLaughlin
Deputy Assistant Secretary (Federal Finance) ..	John Schmidt
Director, Office of Government Financing .....	Francis X. Cavanaugh
Director, Office of Market Analysis and Agency Finance .....	Roland H. Cook
Director, Office of Revenue Sharing .....	Jose P. Lucero
Assistant Secretary (Public Affairs) .....	Joseph Laitin
Deputy Assistant Secretary .....	Everard Munsey

## BUREAU OF ALCOHOL, TOBACCO AND FIREARMS

Director .....	G. R. Dickerson
Deputy Director .....	Stephen E. Higgins
Assistant Director (Administration) .....	Barbara Pomeroy
Assistant Director (Planning and Evaluation) .....	Michael H. Lane
Assistant Director (Criminal Enforcement) .....	John Krogman (acting)
Assistant Director (Internal Affairs) .....	Donald Zimmerman
Assistant Director (Regulatory Enforcement) .....	William T. Drake
Assistant Director (Technical and Scientific Services)	Michael Hoffman
Chief Counsel .....	Marvin J. Dessler

## OFFICE OF THE COMPTROLLER OF THE CURRENCY

Comptroller of the Currency .....	John G. Heimann
Executive Assistant to the Comptroller .....	James W. Montanari
Senior Advisor to the Comptroller .....	Charles E. Lord
Senior Deputy Comptroller .....	Lewis G. Odom
Senior Deputy Comptroller for Operations .....	H. Joe Selby
Senior Deputy Comptroller for Policy Planning ....	Cantwell F. Muckenfuss
Senior Deputy Comptroller for Bank Supervision ...	Paul M. Homan
Deputy Comptroller (Special Surveillance) .....	William E. Martin
Deputy Comptroller (Administration) .....	James T. Keefe
Deputy Comptroller (Specialized Examinations) ....	Dean E. Miller
Deputy Comptroller (Research and Economic Programs) .....	William A. Longbrake
Deputy Comptroller (Interagency Coordination) ....	David C. Motter
Deputy Comptroller (Multinational Banking) .....	Billy C. Wood
Deputy Director Comptroller (Customer and Community Programs) .....	Jo-Ann Barefoot
Chief National Bank Examiner .....	Edmund Zito
Special Assistant to the Comptroller .....	George A. Cincotta
Special Assistant to the Comptroller .....	Susan Wagner
Special Assistant to the Comptroller .....	Richard M. Kovarik
Special Assistant to the Comptroller .....	Stuart J. Gordon
Special Assistant to the Comptroller (Congressional Affairs) .....	Donald A. Melbye
Director, Communications .....	Leonora S. Cross
Director, Bank Organization and Structure .....	James V. Elliott

## UNITED STATES CUSTOMS SERVICE

Commissioner of Customs .....	Robert Chasen
Deputy Commissioner .....	William T. Archey
Assistant Commissioner (Border Operations) .....	Charles C. Hackett, Jr.



Assistant Commissioner (Office of Commercial Operations) .....	Alfred R. DeAngelus
Director (Office of Regulations and Rulings) .....	Donald W. Lewis
Comptroller .....	Jack Lacy
Director (Office of Investigations) .....	Martin White (acting)
Assistant Commissioner (Office of Management Integrity) .....	George C. Corcoran, Jr.
Chief Counsel .....	Richard H. Abbey

## BUREAU OF ENGRAVING AND PRINTING

Director .....	Harry R. Clements
Deputy Director .....	Larry E. Rolufs (acting)
Assistant Director (Administration) .....	Robert J. Leuver
Assistant Director (Operations) .....	Larry E. Rolufs
Assistant Director (Research and Engineering) .....	Milton J. Seidel

## FEDERAL LAW ENFORCEMENT TRAINING CENTER

Director .....	Arthur F. Brandstatter
Deputy Director .....	David W. McKinley
Assistant Director for Resource Management .....	William M. Kelso
Assistant Director for Faculty Management .....	David G. Epstein
Assistant Director for Program Management .....	Ray M. Price
Assistant Director Special Training Division .....	John J. O'Sullivan
Assistant Director (Washington Liaison Office) .....	John C. Dooher
Chief, Training Support Division .....	John Osborne

## BUREAU OF GOVERNMENT FINANCIAL OPERATIONS

Commissioner .....	William E. Douglas
Deputy Commissioner .....	(Vacancy)
Assistant Commissioner, Administration .....	(Vacancy)
Assistant Commissioner, Comptroller .....	(Vacancy)
Assistant Commissioner, Banking and Cash Management .....	Russell D. Morris
Assistant Commissioner, Disbursements and Claims .....	Michael D. Serlin
Assistant Commissioner, Government-wide Accounting .....	John O. Turner
Associate Commissioner .....	Lester Plumley

## INTERNAL REVENUE SERVICE

Commissioner .....	Jerome Kurtz
Deputy Commissioner .....	William E. Williams
Assistant Commissioner (Taxpayer Service and Returns Processing) .....	M. Eddie Heironimus
Assistant Commissioner (Resources Management) ..	Joseph T. Davis
Assistant Commissioner (Compliance) .....	P. E. Coates
Assistant Commissioner (Employee Plans and Exempt Organizations) .....	S. Allen Winborne
Assistant Commissioner (Inspection) .....	Robert L. Rebein
Assistant Commissioner (Planning and Research) ...	Russell E. Dyke
Assistant Commissioner (Technical) .....	Gerald G. Portney
Assistant Commissioner (Data Services) .....	Donald J. Porter
Chief Counsel .....	N. Jerold Cohen

## BUREAU OF THE MINT

Director .....	Stella Hackel Sims
Deputy Director .....	Allen J. Goldman
Assistant Director for Budget and Finance .....	Joseph M. Wagner
Assistant Director for Marketing .....	Francis B. Frere

Assistant Director for Production .....	Galen D. Dawson
Assistant Director for Personnel .....	James J. Mulcahy
Assistant Director for Technology .....	Alan J. Goldman
Assistant Director for Management Services .....	Judith L. Wagner

## BUREAU OF THE PUBLIC DEBT

Commissioner .....	H. J. Hintgen
Deputy Commissioner .....	William M. Gregg
Assistant Commissioner (Washington) .....	Kenneth W. Rath
Assistant Commissioner (Field) .....	Martin French
Chief Counsel .....	Calvin Ninomiya

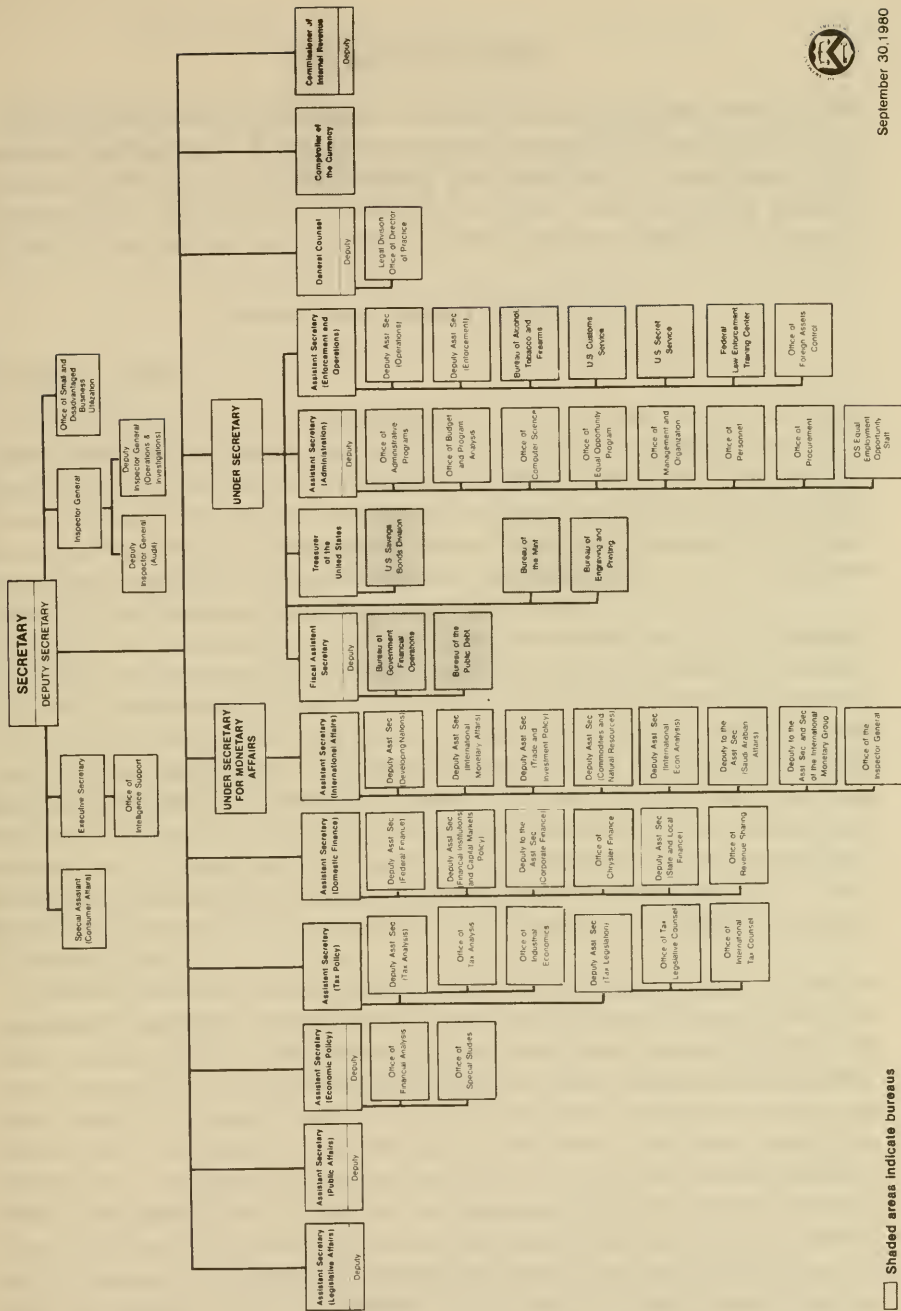
## UNITED STATES SAVINGS BONDS DIVISION

National Director .....	Azie T. Morton
Deputy National Director .....	Jesse L. Adams, Jr.
Director of Sales .....	Walter R. Niles
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## UNITED STATES SECRET SERVICE

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**ORGANIZATION OF THE DEPARTMENT OF THE TREASURY**







# INTRODUCTION

This introduction reviews major domestic and international developments which affected areas of Treasury interest and responsibility during fiscal 1980. Detailed information on the operating and administrative activities of the Department is provided in the text of the report and supporting exhibits. Statistical information may be found in the separate Statistical Appendix.

## DOMESTIC DEVELOPMENTS

### Economic Activity

The economic expansion which began in early 1975 was finally interrupted during 1980. An extremely brief period of contraction, reflected in only a single quarter of decline in real output, took place during the fiscal year. By the end of the fiscal year, real growth had resumed, and the shortest recession of the postwar period had apparently drawn to a close. However, interest rates were rising rapidly at an early stage of the expansion and the near-term outlook for the economy remained somewhat uncertain.

During the fiscal year, real gross national product declined by 1.5 percent, and prices, as measured by the fixed-weight GNP deflator, rose by 9.8 percent. The output pattern during the year was rather uneven. Real GNP grew slowly during the first half of the fiscal year, at about a 1½-percent annual rate, and then dropped sharply at a 9.6-percent annual rate in the spring and early summer, before resuming growth at about a 1-percent annual rate in the final quarter of the fiscal year. Inflation was running at about a 9½-percent annual rate early in the fiscal year. It rose to an 11-percent annual rate in the early months of calendar 1980, when consumer prices rose temporarily at even higher rates, and then fell back close to the 9½-percent range again by the end of the fiscal year.

Domestic economic developments were strongly affected by a second oil price shock, analagous to that experienced in 1974. By early January 1980, the world price of oil had reached about \$28 per barrel, more than double the level of a year earlier. As the effect of higher oil prices fed through to the domestic price level in the early months of 1980, the rate of inflation worsened substantially. In January and February, there were also some signs that inflation was beginning to spread beyond the energy and home financing areas. The annual rate of inflation as measured by the CPI, which many consider a flawed indicator of price change, rose temporarily to 18 percent, and inflationary expectations intensified greatly. Serious disturbances in domestic financial markets developed in February and early March. Interest rates rose sharply, and the functioning of some long-term private financial markets seemed to be threatened.

In response to these developments, the administration announced new actions for intensified fiscal and credit policies, reinforcing the programs of restraint already in place. In the fiscal area, fiscal 1981 budget proposals were

revised after extensive consultation with congressional leadership. The revisions were designed to eliminate some \$17 billion in programmatic expenditures and to bring the budget into balance. In addition, various measures to improve tax collections and conserve energy were proposed or initiated.

Strong steps were taken in the monetary area. Under the terms of the Credit Control Act of 1969, the President authorized the Federal Reserve to exercise new, temporary power to slow the growth of consumer and business borrowing. In the consumer credit area, the Federal Reserve imposed a special deposit requirement of 15 percent on any expansion of credit provided by credit cards, other forms of unsecured revolving credit, and personal loans. In addition, the Federal Reserve took further steps to restrain domestic credit expansion, including an increase in the marginal reserve requirement on managed liabilities and a surcharge for large banks on borrowings through the Federal Reserve discount window.

The actions taken at mid-March were extremely powerful. Indeed, the controls on consumer credit quickly led to a drastic reduction of consumer borrowing and spending. Outstanding consumer credit was reduced by \$9.5 billion between March and July when the credit control program was lifted. Consumer spending in real terms declined at a 10.6-percent annual rate in the March-June period—the largest such quarterly decline in the postwar period. The resulting economic adjustment was sharp but exceedingly brief. Real GNP fell at a 9.6-percent annual rate in the second quarter of the calendar year, but growth then resumed at a modest pace in the final quarter of the fiscal year.

The automobile and housing sectors were particularly hard hit. Domestic auto sales peaked at an 8.6-million-unit annual rate in January and hit a low of 5.2 million units by June. Production was cut sharply to keep inventories in line with falling sales, and indefinite layoffs in the auto industry reached 250,000 by midsummer. Housing activity was already declining in response to rising interest rates at the beginning of the fiscal year, and mortgage markets virtually ceased to function temporarily in the spring as mortgage rates reached 16 percent and higher in some sections of the country. Housing starts fell to an annual rate of 906,000 units in May, a decline of more than 45 percent from the level of starts at the beginning of the fiscal year.

With the economy falling rapidly in the period following the mid-March actions, many private forecasts shifted in the direction of deep recession. The unemployment rate was expected by many observers to reach the 9-percent level experienced in 1975. The unemployment rate did rise sharply from 6.2 percent in March to 7.8 percent in May but then drifted down and reached 7.5 percent by the end of the fiscal year. Following the mid-March credit measures, interest rates fell very sharply, and normal flows of credit were quickly restored. The 3-month Treasury bill was 15¼ percent just prior to the announcement of the budget cuts and new credit restraints. By mid-June, the 3-month bill auctioned below 6¼ percent. The bank prime lending rate which

peaked at 20 percent fell to 11 percent by late summer and mortgage rates fell back to the 12½-percent range.

The recovery of consumer and other spending sensitive to interest rates was a major factor in the economic turnaround which began in the summer and was readily apparent in a range of statistics by the end of the fiscal year. Domestic auto sales were running about 30 percent above their midsummer lows, housing starts were up 73 percent, and a general economic recovery was underway.

Despite the effectiveness of the measures taken in mid-March and the ensuing economic rebound, there were still some major uncertainties regarding the economic outlook at the close of the fiscal year. Inflation was relatively undiminished with the fixed-weight GNP deflator growing at a 9½-percent annual rate, about the same as at the beginning of the fiscal year. Interest rates were rising again with the 3-month bill rate above 11 percent and the prime rate at 13½ percent. The monetary aggregates were growing rapidly and threatening to run above target despite determined efforts by the Federal Reserve. The prospects for a sustained economic expansion were somewhat clouded in the face of these financial developments, although the economy was still showing considerable forward momentum.

Late in the fiscal year, the administration proposed an economic revitalization program to deal with longer run economic problems. The administration intended to seek legislative action on the program in early 1981. The proposals included enlarged incentives to spur private capital formation; public investment in the energy area; formation of an Economic Revitalization Board with representatives from industry, labor, and the public; transitional aid to regions and groups; and selective tax reduction for individuals.

Despite the economic adjustment occurring during fiscal 1980, substantial economic gains had been made during the 4 fiscal years, 1977–80. During that period, real GNP rose 10½ percent, real disposable income per capita was up 7.2 percent, corporate profits after inventory valuation and capital consumption adjustments were 24.7 percent higher, and 9.3 million more Americans were employed. Inflation remained a major problem, however, to which a final solution had not yet been found.

## **Inflation**

The general pattern of price developments during the fiscal year was a pronounced acceleration of inflation up to the time of the imposition of the credit control measures at mid-March followed by some deceleration during the brief period of the economic decline. By the end of the fiscal year, however, inflation was apparently beginning to speed up again. The consumer and producer price indexes followed a roughly similar course during the fiscal year. By 3-month periods, the annual rates of increase in consumer prices were: 13.7, 18.1, 11.6, and 7 percent. For producer prices, the comparable rates of increase were: 13.3, 19.3, 6.7, and 12.2 percent. Both series are somewhat more volatile on a short-term basis than the fixed-weight GNP deflator which



began and ended the fiscal year at about a  $9\frac{1}{2}$ -percent annual rate of increase, after reaching a peak quarterly rate during the fiscal year of about an 11-percent annual rate.

A discouraging feature of inflationary developments, aside from short-term upswings, was the steady upward drift in the inflation rate over time. The fixed-weight GNP deflator—a comprehensive and relatively stable measure—has risen steadily over the 4 most recent fiscal years, from  $6\frac{1}{2}$  percent at the beginning of the period to about  $9\frac{3}{4}$  percent during fiscal 1980. By yearend, most economic estimates of the underlying or “core” rate of inflation had reached the 9-percent range with no immediate prospects in view for dramatic improvement.

The inflationary process had become deeply imbedded in economywide compensation and costs. During fiscal 1980, total compensation per hour in the private nonfarm business sector rose 9.9 percent. Productivity actually fell by 0.7 percent; and, as a result, unit labor costs rose by 10.7 percent.

Productivity performance has become a problem in its own right, not only because of a short-term impact on inflation, but also because of a deterioration in longer term performance. Between 1948 and 1968, productivity in the private nonfarm business sector rose at a 2.6-percent annual rate. In the 1968–73 period, productivity grew at a 1.7-percent annual rate, before falling off further to only a 0.5-percent rate of advance between 1973 and 1979. The reasons for this decline are complex and the subject of continuing inquiry, but a slowdown in growth of the net capital stock appears to have been an important contributing factor. Therefore, there is general agreement that steps to increase the incentives for saving and capital formation are probably an important element in any long-term effort to contain inflation and raise productive potential.

### **The Budget and Fiscal Developments**

The budget estimates for fiscal 1980 presented in January 1980 called for outlays of \$563.6 billion and receipts of \$523.8 billion, leaving a deficit of \$39.8 billion. A reestimate was made in March, taking account of the mid-March fiscal measures, which lowered the deficit estimate to \$36.5 billion. By the time of the midsession budget review in July, the budgetary outlook had deteriorated noticeably. Receipts and outlays were affected by the short but sharp recession, and a range of legislative and other developments had also affected the situation. Outlays were reestimated at \$578.8 billion and receipts at \$517.9 billion, yielding a deficit of \$60.9 billion. The final results for the fiscal year were fairly close to the midsession estimates: outlays of \$579 billion and receipts of \$520 billion resulting in a deficit of \$59 billion.

Off-budget net outlays for fiscal 1980 were somewhat smaller than anticipated. In the January budget submission, such outlays were estimated at \$16.8 billion. The actual figure was \$14.2 billion. The smaller than expected outlays were largely attributable to Federal Financing Bank outlays nearly \$2

billion below the January estimate, and a swing in the Postal Service from an expected deficit of \$0.2 billion to a surplus of \$0.4 billion.

### **Domestic Finance**

The volume of funds raised in the U.S. credit markets declined substantially in fiscal 1980 as the result of the recession, credit controls, and high interest rates. With the budget deficit increasing, Federal demands for credit about doubled from the 1979 level, but the rise was far outweighed by the significant reduction in non-Federal borrowings.

At the start of the fiscal year, after the adoption by the Federal Reserve of a restrictive credit policy in October 1979, total credit demands slackened noticeably. A subsequent leveling off in interest rates brought a strong revival of credit demands in the winter months, but the imposition of tighter conditions along with a credit restraint program in February and March, together with the steep recession which ensued, drastically curtailed the expansion of credit in the spring quarter. In the summer, however, with the economy recovering and interest rates sharply lower, credit demands strengthened materially, even though credit was tightened again toward the end of the fiscal year.

The expansions and contractions of credit demands during 1980 mirrored, and were reflected in, developments in money supply growth and interest rates as well as in economic activity. Money supply growth slowed appreciably in the final calendar quarter of 1979 and remained relatively subdued through the first calendar quarter of 1980. This slowdown was followed by sharp reductions in the measures of transaction balances, M1-A and M1-B, in the second calendar quarter in response to the abrupt declines in economic activity and credit demands. In the final quarter of the fiscal year, however, the growth of the money supply measures accelerated to record proportions, thereby triggering additional credit-tightening measures. For the fiscal year as a whole, the rate of growth of M1-A (currency and demand deposits), at 4.9 percent, was about the same as in the prior fiscal year. M1-B, which includes, in addition, other checkable deposits (ATS and NOW accounts), grew at a somewhat slower pace than in the year before—6.4 percent versus 8 percent—as transfers from savings accounts to ATS checkable accounts were somewhat smaller than during the initial rapid rush when such accounts were permitted in 1979.

Wide movements in interest rates also characterized fiscal 1980. In the opening quarter, sharp increases in interest rates accompanied the tighter credit policy imposed in October. By the end of December, however, the markets had settled down and interest rates had subsided somewhat. As the first calendar quarter progressed and credit demands strengthened, the even more drastically restrictive credit measures imposed, including credit controls, raised interest rates to unprecedented levels. The Federal funds rate, which had been fluctuating around 11½ percent at the opening of the fiscal year and had reached a weekly average of over 15½ percent in October before falling

back to about 13½ percent at the turn of the year, soared to a peak of around 19½ percent. Money market rates fluctuated in a similar pattern, at somewhat lower levels, and the prime rate, which had started the fiscal year at 13¼ percent, peaked at 20 percent in early April. The subsequent decline in interest rates, from early April through mid-June, carried them down precipitously to around 9 percent for Federal funds, 11 percent for the prime rate, and 7 to 8½ percent for other money market rates. By the final quarter of the fiscal year, another round of tightening had once again resulted in a swift rise in interest rates, which carried over beyond the close of the fiscal year. At the end of September 1980, Federal funds were trading at around 13¼ percent, the prime rate stood at 13 percent, and other money market rates were fluctuating around 11½ to 12½ percent.

The sharp changes in credit conditions in fiscal 1980 entailed considerable uncertainty for long-term borrowers in both the mortgage and the bond markets. As mortgage rates pushed up in the fall of 1979 and winter of 1980, from around 11 percent to 16 percent, mortgage funds for home sales and construction virtually dried up. The subsequent loosening of credit and improvement in savings flows brought mortgage rates down to a low of around 12 percent in July–August. By the end of the fiscal year, the consequent recovery which had taken hold in the housing market early in the July–September quarter was being threatened by further credit tightening and rising mortgage rates.

The bond markets were also severely affected by the runup in bond yields in February and March, so much so that some market commentators felt that it would be virtually impossible to sell long-term bonds in the foreseeable future. Bond yields rose from around 9–9½ percent at the start of the fiscal year to peaks of around 13–14½ percent in the February–March period. As the level of bond yields subsided thereafter reaching lows of around 9½–11 percent in June, corporate bond financing mounted to record proportions in the second calendar quarter. At the end of the final quarter of the fiscal year, the sharp rise in the yield on new Aa corporate utility issues from 11½ percent at the end of June to 14 percent at the end of September was already inducing another severe curtailment of new issue activity and an atmosphere in which it was again becoming difficult to sell long-term bonds.

In particular sectors, Treasury borrowing from the public through Treasury securities increased from \$35.2 billion in fiscal 1979 to \$71 billion in fiscal 1980. The \$87.4 billion increase in interest-bearing marketable debt was much larger than the total increase in 1980 because of a sharp (\$13.9 billion) reduction in nonmarketable debt outstanding. Savings bonds and notes declined by \$7.8 billion, foreign nonmarketable issues by \$5.2 billion, and State and local issues by \$0.9 billion. Most of the Treasury net marketable borrowings were of shorter term in 1980, compared with the preponderance of bonds (68 percent) in 1979. The Treasury's authority to issue bonds had been enlarged at the start of the fiscal year, but the sharp step-up in requirements, together with the uncertain state of the bond markets, served to hold the net



increase in bonds in 1980 to \$12.7 billion compared with \$14.7 billion in 1979. Offerings in the 15-year and 30-year maturity categories continued to be made on a quarterly basis. Marketable Treasury notes (with maturities of as long as 10 years) accounted for \$36.7 billion, or 41.7 percent, of the net increase in interest-bearing marketable debt, while marketable Treasury bills (with maturities of 3 months to 1 year) accounted for \$38.5 billion, or 43.8 percent of the total.

Business demands for credit dropped by 17 percent in the fiscal year to a total of \$130.9 billion, of which \$37.8 billion took the form of securities, \$40 billion represented mortgages, and \$53.1 billion short-term credit. Bond borrowings were considerably larger than in fiscal 1979 because of the huge total of bonds sold in the second quarter of the calendar year when interest rates had subsided. Mortgage borrowings by business receded materially, while funds raised through short-term debt were down even more substantially. Bank loans increased strongly in the first and third calendar quarters but were paid down in the second, while open market paper was paid down in the third. Over the fiscal year as a whole, however, short-term business borrowings were almost evenly divided between bank loans and other types of borrowings.

State and local government bond borrowings increased by 11 percent in fiscal 1980 to reach \$18.1 billion. The total would have dropped but for an enhanced issuance of tax-exempt housing bonds, which totaled \$12.6 billion, compared with the previous year's total of \$7 billion. Foreign borrowings by governments and business fell off sharply to \$21.6 billion from the \$37.6 billion of the previous year. A drastic cut in bank lending was accompanied by reduced net issuance of both bankers' acceptances and bonds.

The remaining category of nonfinancial credit demands, consumer borrowing, plummeted in 1980, as consumers tightened their budgets, cutting back severely on mortgages and installment credit in response to credit controls and high interest rates. Net new home mortgages issued dropped from \$110.1 billion in fiscal 1979 to \$80 billion in 1980, or by 27.4 percent, while net consumer credit extended dwindled from \$48.3 billion in 1979 to \$2.9 billion in 1980. All told, consumer borrowing, comprising home mortgages, installment, and miscellaneous borrowing, totaled \$168.4 billion in 1980, down by over one-third from the 1979 total.

In sum, credit demands from the four major groups of nonfinancial non-Federal borrowers were greatly reduced in fiscal 1980. The total of \$278.1 billion represented a decline of 27 percent from the 1979 total of \$379.7 billion. In addition, credit demands from financial borrowers as a group (Federal agencies, finance companies, savings and loan associations, fire and casualty insurance companies, and commercial banks) were substantially curtailed, dropping by 35 percent to \$74.3 billion. As a result, even with the increase in Federal borrowings, the total volume of funds raised in the credit markets in fiscal 1980, at \$423.4 billion, was \$106.2 billion smaller than the fiscal 1979 total.

The corresponding large reduction in the sources of funds was most extreme for the banking and household sectors, although savings and loan associations, mutual savings banks, and credit unions also provided significantly fewer funds for the purchase of credit instruments in 1979. The new 2 $\frac{1}{2}$ -year certificates permitted to be offered by thrift institutions and commercial banks in January 1980 attracted \$75.5 billion of funds, but money market certificates (in denominations of \$10,000) increased by a smaller amount, \$142.2 billion, than the \$170.7 billion increase of 1979, with the result that the cushion against the drain on savings inflows from regular accounts provided thereby was smaller. On the other hand, the net increase in money market funds of \$42.5 billion was considerably larger than the \$26.5 billion of the prior year.

### **Taxation Developments**

Tax policy during fiscal 1980 reflected the simultaneous needs to reduce U.S. reliance on uncertain foreign energy sources, contain inflation, and maintain employment.

The Crude Oil Windfall Profit Tax Act of 1980 (Public Law 96-223, proposed April 26, 1979) was enacted April 2, 1980. The windfall profit tax is a graduated set of taxes applied to domestically produced oil that will be used to finance the burden of higher energy costs of low-income individuals, to finance programs to encourage energy conservation, and to reduce income taxes. As part of the act, increased solar and business tax subsidies are provided for conservation investments and the production of fuels from renewable and exotic sources. Included in the act were three income tax provisions: A \$200 exclusion for interest and dividends (\$400 for married couples), repeal of carryover basis, and changes to LIFO accounting rules. The tax is to phase out when net receipts reach \$227.3 billion, but beginning no later than January 1, 1991, or earlier than January 1, 1988.

Reduction in inflation was the first priority of domestic economic policy during 1980. The budget for fiscal 1981, presented in January 1980, proposed a tight fiscal policy coupled with programs to alleviate structural causes of inflation. The tax-related measures provided for increased receipts of \$6.4 billion in fiscal 1980 and \$26 billion in fiscal 1981.

The cash management initiatives in the budget balanced the benefits of collecting taxes closer to the time when tax liabilities accrue against the higher administrative costs. Overall, these initiatives would have increased receipts and decreased Government borrowing costs by \$5.1 billion in fiscal 1981 and \$6.7 billion in fiscal 1982. Two of the four proposals that can be implemented administratively were scheduled to become effective by January 1981.

In March 1980, as part of his anti-inflation program, the President announced two revenue-increasing measures: A gasoline conservation fee of \$4.62/barrel on imported crude oil and a proposal to withhold income tax on interest and dividends. These measures would have increased receipts in fiscal 1981 by approximately \$13 billion. No new tax would have been imposed

upon dividend and interest income. The proposal was designed primarily to avoid the inequities and higher tax rates that occur when some taxpayers do not report all their income. Taxpayers were estimated to have underreported interest and dividend income in 1979 by about \$16 billion and thereby underpaid taxes by approximately \$3.6 billion.

In August, the President announced the details of his economic revitalization program. This program was designed to create half a million jobs by the end of 1981 and a total of 1 million jobs by the end of the following year. Cost-reducing and productivity-enhancing provisions were incorporated to boost investment and speed the recovery of the faltering economy. The tax provisions included: Liberalization and simplification of depreciation, making the investment tax credit partially refundable, providing an individual tax credit to offset social security tax increases, liberalization of the earned income credit, a targeted investment credit to assist depressed areas, rapid amortization of startup costs for small business, and some relief from the marriage penalty. These provisions altogether would have reduced tax liability by \$27.6 billion in calendar 1981, rising to \$58.3 billion in 1985.

## INTERNATIONAL AFFAIRS

### The Year in World Finance

During fiscal 1980, rates of inflation in consumer prices in industrial countries rose, reaching a year-on-year average increase of about 11½ percent in September 1980. This rise occurred despite a marked decline in the pace of real economic growth. Payments positions worsened for most industrial and developing countries as the combined current account surpluses of the oil-exporting countries rose sharply as a result of increases of about 75 percent in prices for crude petroleum. With lower real growth, the U.S. position was expected to move from near balance in calendar 1979 to a current account surplus of about \$5 billion in calendar 1980. Despite somewhat slower growth rates in 1980, large current account deficits were anticipated for the Federal Republic of Germany (about \$15 billion), Japan (more than \$10 billion), Italy (about \$9 billion), and France (about \$9 billion), as these countries absorbed a large share of the payments impact of higher prices for oil. Although exchange rates showed considerable movement at times during the fiscal year, the dollar's average level in terms of major foreign currencies at the end of the year was about the same as at the beginning.

During the year, short-term interest rates for the U.S. dollar were extremely volatile. In London, Eurodollar rates rose about 3 percent in the fourth quarter of 1979, to 14¾ percent, and averaged nearly 20 percent in March 1980, before declining to 9¾ percent in June 1980. In August, this key international rate rose again and averaged nearly 14 percent in September 1980. Rates in other leading currencies moved more slowly to moderately higher levels, ending the fiscal year in a broad range from about 9 percent in Germany to 17 percent in Italy.



The sharp swings in dollar interest rates were related to rapidly changing expectations as to future inflation rates; to rapid changes in the pace of real economic activity in the United States; and to the adoption early in October 1979 of new criteria for monetary policy by the Federal Reserve. These criteria placed primary emphasis on the rate of growth of monetary aggregates and thus led to wider fluctuations in U.S. short-term interest rates than did previous policies.

In fiscal 1980, net changes in the U.S. trade balance and the U.S. current account were small as compared with the previous year. Although petroleum imports rose by over \$25 billion to nearly \$80 billion, due to a year-over-year increase in average oil import prices of about 75 percent, the trade deficit worsened only by about \$3 billion, to a level of about \$30 billion. An increased surplus on net invisibles (international services and transfer payments) offset part of this, leaving a deficit in the current account of about \$2 billion. Recorded net capital outflows of private capital nearly doubled and were almost offset by inflows in the categories of recorded official capital and the statistical discrepancy, which is believed to include unrecorded capital movements.

Large increases in the current account deficits of most other industrial countries and changing relationships among interest rates in the United States and major countries were two of the many factors affecting the foreign exchange markets. A pronounced dip in the dollar value of the deutsche mark (DM) and the Swiss franc occurred during the first 4 months of 1980 when dollar interest rates rose sharply, followed by a subsequent recovery when dollar rates declined. During the fiscal year as a whole, the dollar appreciated by 4 percent in terms of DM and depreciated by nearly 8 percent in terms of British sterling and by about 6 percent in terms of Japanese yen. On a trade-weighted basis, the dollar rose very slightly over the 12-month period in terms of the currencies of the members of the Organization for Economic Cooperation and Development (OECD) and likewise in terms of special drawing rights (SDR's).

The Federal Reserve and the Treasury intervened to counter disorderly conditions in the exchange market, making net purchases of nearly \$4 billion equivalent of foreign currencies during the fiscal year. These acquisitions were used to restore balances drawn down in earlier periods and to repay swap debts incurred in earlier interventions. [By the end of October, all outstanding swap debts had been repaid.]

The price of gold was highly volatile, rising during the year from about \$400 per ounce to about \$670, after reaching a peak of about \$850 per ounce early in 1980.

During the fiscal year, much attention was given to the problems of recycling funds from the capital surplus oil exporters to the deficit countries, particularly to those developing nations that have been borrowing heavily from the commercial banking system. The current account surplus of the oil-

exporting countries was projected to rise about \$50 billion in calendar 1980, to a total of about \$110 billion.

Over the 2-year period 1979–80, about two-thirds of the offsetting deficits corresponding to the \$170 billion combined current account surpluses of the members of the Organization of Petroleum Exporting Countries (OPEC) fell upon the industrial countries as a group; no less than a quarter of the OPEC surpluses was financed by deficits of the Federal Republic of Germany and Japan.

The combined current account deficits of non-OPEC developing nations as a group (after allowing for unrequited inward transfers of official funds) were expected to rise from the calendar 1979 figure of about \$40 billion to a little more than \$60 billion in calendar 1980. Most of this calendar 1980 deficit was expected to be financed by private capital flows, but the cost of servicing foreign borrowing was rising and in some cases bank credits were more difficult to obtain at the end of the fiscal year. Some countries have encountered difficult financial problems, and a growing number of countries have had recourse to the International Monetary Fund (IMF) for financing to support their adjustment efforts.

Real rates of growth declined in the OECD countries from an estimated  $3\frac{1}{2}$  percent per annum in calendar 1979 to about  $1\frac{1}{2}$  percent in calendar 1980. Among major industrial countries, calendar 1980 estimated real growth rates range widely: A negative 3 percent in the United Kingdom, zero in the United States, a positive 2 percent in Germany, and more than 5 percent in Japan. The non-OPEC developing nations as a group were expected to grow by about 5 percent in 1980, an average rate that has been maintained since 1976.

Inflation continued to resist policies of restraint, but a somewhat slower pace was achieved in the July–September quarter, after the year-over-year rise of consumer prices in the industrial countries as a group had gone from an average rate of about  $9\frac{1}{2}$  percent in the third quarter of 1979 to about  $12\frac{1}{2}$  percent in the second quarter of 1980. Germany, Japan, Benelux, and Switzerland continued to record substantially lower than average rates of advance in consumer prices.

International reserves of countries, excluding gold but including European currency units (ECU's) and SDR's, rose by about 17 percent during the fiscal year to a total of \$405 billion. This was about the same percentage rate of growth as in the previous fiscal year. In value terms, yearend reserves were equivalent to about 22 percent of the value of annual global imports (excluding figures for the centrally managed economies of Eastern Europe and China). Gold reserves are valued at different dollar prices by major holders and change very little in physical quantity. Accordingly, the total excluding gold seems the most appropriate figure to use in measuring changes in reserves.

## International Monetary Affairs

As the U.S. member of the Board of Governors of the IMF, Secretary Miller headed the U.S. delegations to the semiannual meetings of the Interim Committee of the Board of Governors of the International Monetary Fund, held in Hamburg in April and in September in Washington, and to the annual meeting of the full Board of Governors in Washington in September 1980. In its April meeting, the Interim Committee was especially concerned with the dramatic and widespread rise in rates of inflation and also with the prospective increases in the level of payments deficits of the nonoil developing countries caused by sharply higher oil prices. Despite the slowdown in growth, particularly in the industrial countries, the Committee agreed that top priority should continue to be given to the fight against inflation. Great importance was attached to avoiding secondary repercussions of the oil price increases on wages, incomes, and prices. On the recycling issue, the Interim Committee agreed that the IMF should stand ready to play a major role in the adjustment and financing of payments imbalances. Although the Fund was relatively liquid at the time, the Committee encouraged the Managing Director of the IMF to start discussions with potential lenders to supplement its resources. The Committee discussed but did not resolve important outstanding issues that had emerged from the work of the Executive Board of the IMF on a plan for a "substitution account," in which countries wishing to diversify their reserves might place part of their reserves against claims on the account.

In September, the Governors again emphasized the same two monetary problems—inflationary expectations and recycling. They cautioned against any premature shift to expansionary monetary and fiscal policies. They also welcomed the IMF Executive Board approach of making available larger amounts of financing than in the past to members making strong efforts to correct their payments problems. While agreeing on the need for IMF borrowing during the next few years, the Committee stressed its view that the Fund should continue to place primary reliance on quota subscriptions as a source of financing. The Committee also noted the work of the Executive Board on a subsidy to low-income borrowers from the IMF and on future allocations of SDR's. The decision to redefine the SDR as a basket of 5 major currencies, instead of 16 currencies, as of January 1, 1981, was welcomed. It was expected to help promote the use of SDR-denominated claims by private as well as public holders. The proposal for a substitution account in the Fund was not actively pursued, but the Committee reiterated its intention to continue to study that subject.

Legislation authorizing participation by the United States in the seventh annual review of quotas was completed, but the requisite appropriation of SDR 4.2 billion was still pending at the end of the fiscal year. [In December, the necessary legislative action on this appropriation was completed, and the United States formally consented to the quota increase.]

The Treasury continued to cooperate with the Federal Reserve in intervening as necessary to counter disorderly conditions in the exchange



market. The Treasury also added to its foreign exchange resources for this purpose by borrowing DM 4,025 million (\$2,287 million) in DM-denominated notes issued in the German market in November 1979 and January 1980. In October 1979, Treasury gold sales were made flexible in amounts and timing, and under this more flexible policy the last sale held during the fiscal year was carried out on November 1, 1979. In July 1980, the Treasury commenced sales to the public of commemorative gold medallions pursuant to the American Arts Gold Medallion Act of 1978.

### **The International Monetary Group**

This interagency group met from time to time at the call of the Under Secretary for Monetary Affairs or, after that position became vacant in February 1980, the Assistant Secretary (International Affairs), to review current and prospective problems of the international monetary system and to help establish positions to be taken by U.S. representatives in the IMF and in other fora for discussing and negotiating international monetary matters.

### **Developing Nations**

Treasury has taken the lead in negotiating U.S. participation in increases in capital for the Inter-American Development Bank (IDB) and in replenishments of the concessional lending resources for the International Development Association (IDA) and the concessional loan windows of the IDB, the Asian Development Bank (ADB), and the African Development Fund (AFDF).

During 1980, Congress approved authorizing legislation for U.S. subscriptions and contributions to the regional banks, but at levels 10 and 15 percent below the negotiated amounts for the IDB and the ADF, respectively. Although legislation for U.S. subscriptions to the sixth replenishment of IDA (IDA VI) was submitted to Congress during 1980, it was not approved.

The Congress also approved a continuing resolution providing a total of \$1.5 billion for U.S. subscriptions and contributions to these multilateral development banks (MDB's) through use of budget authority and program limitations. As part of this resolution, proposals for enacting "program limitations on callable capital" for IBRD and ADB capital were also approved. These have the effect of placing congressional limits on the loan programs of those MDB's that are supported by market borrowings related to their callable capital rather than actually appropriating such capital.

At the annual meetings of the World Bank group and the IMF at the end of September 1980, Secretary Miller gave U.S. support to implementation of a new World Bank lending program to provide about \$14 billion in loans through 1985 in support of energy development projects totaling approximately \$56 billion. This program could potentially add the equivalent of 2.5 million barrels of oil per day to world energy supplies. The Secretary also encouraged the Bank's new program to support medium-term structural adjustment programs in member countries through lending designed for this purpose and

coordinated closely with the IMF. It is hoped that such loans will help in coping with increasingly difficult recycling problems of developing nations. In addition, Secretary Miller also approved the Bank's continuing efforts in the sphere of population and urged that the Bank continue emphasizing projects in which benefits more directly reach the poor and that the Bank allocate a larger share of its lending to the poorer borrowing countries.

In other aspects of U.S. relations with developing nations, Treasury took part in international debt rescheduling negotiations with four countries—Sierra Leone, Sudan, Turkey, and Zaire. These countries faced critical payments problems and had sought assistance from the IMF in carrying out adjustment programs. In the case of Turkey, a consortium of members of the OECD also pledged about \$1.2 billion of assistance during Turkish fiscal year 1980–81 to meet the severe financial crisis in that country.

Following the seizure of the Americans in Iran and threats by that Government that it would not honor its financial obligations to U.S. citizens and entities, the U.S. Government responded with a series of actions including the blocking of Iranian assets on November 14, 1979.

During the year, the Secretary took part in two meetings of the Development Committee, a group consisting of Governors of the IMF and the World Bank. The April meeting reviewed proposals in the "Program of Immediate Action" prepared by the Group of 24 leading developing countries. In addition, there was a preliminary discussion of the extensive report on development financing made by the Brandt Commission that had been initiated by the President of the World Bank. The Development Committee urged increased public and private financing to meet payments deficits swollen by oil price increases and mounting debt service charges.

In September 1980, the Committee foresaw a further increase in the current account deficits of the oil-importing developing countries in calendar 1981 over the calendar 1980 level. It recognized that, along with strong support from industrialized countries and oil exporters, vigorous adjustment efforts were necessary by the developing countries. These efforts should include expansion of exports, new energy production, economy in energy use, and more efficient use of capital, human resources, and imports. The Committee also welcomed the Bank's intention to examine the possibility of an energy affiliate or facility to expand lending operations in the energy sector. The Committee asked the Bank Board to explore promptly ways of enlarging the Bank's lending capacity to take account of world inflation, which has reduced the real value of previously planned lending, as well as to meet prospective new requirements for structural adjustment and energy loans.

### **Natural Resources and Commodities**

Recession, improved conservation, and higher prices for oil brought a 6-percent reduction in the rate of consumption of oil by OECD members at the end of the fiscal year as compared with a year earlier. The average OPEC price rose from about \$20 per barrel in September 1979 to about \$32 per barrel in

September 1980. Treasury policies and programs concentrated on the effects of OPEC price and supply decisions on the U.S. economy; on demand restraint and alternative energy production in the context of U.S. commitments under the International Energy Agency (IEA) and the Venice economic summit; and on energy exploration and development in developing countries. The economic summit emphasized longer term programs to conserve energy and agreements to develop policies for increased production of coal, nuclear, synthetic, and renewable energy resources.

Treasury participated in the Governing Board and subordinate groups of the IEA. Major achievements of the year were the setting of industrial country oil import targets for 1980 and 1985 and a procedure for fixing politically binding ceilings to meet a short-term market disruption. Subordinate groups dealt with emergency questions, consultations on and information gathering on imports and stocks, and long-term cooperation and needs for structural changes in use of oil and coal.

In the sphere of international commodities, further progress was made within the framework of the International Program for Commodities, which was developed at the fourth United Nations Conference on Trade and Development (UNCTAD IV) in 1976 and reaffirmed at UNCTAD V in 1979. The Treasury took an active part in the financial aspects of the Common Fund, for which Articles of Agreement were completed after 4 years of intensive negotiations. The First Account of the Common Fund will facilitate the financing of the buffer stocking operations of the international commodity agreements associated with the Fund. The primary resources derived from associated commodity agreements will be supplemented by up to \$400 million in capital contributed by Common Fund members. A Second Account will be funded by voluntary contributions and used to promote marketing, research, and development; the United States does not plan to contribute to this account in the foreseeable future.

Several significant developments took place in discussions on individual commodities which are likely to mark the cresting of international attention toward new price stabilization agreements. A Natural Rubber Commodity Agreement was negotiated which the United States joined provisionally until such time as Congress completes the appropriations process. Coffee-consuming countries, led by the United States, persuaded the producing countries to end their collusive price arrangement in return for a pledge to activate the economic provisions of the International Coffee Agreement. Also, the United States actively participated in negotiation of new tin and cocoa agreements, although progress in them was disappointing.

In the related field of seabed mineral exploitation, legislation was enacted providing for orderly development of a domestic deep seabed mining industry in a manner consistent with the U.S. position at the Law of the Sea Conference under U.N. auspices.



## Trade and Investment Policy

Treasury took an active part in the implementation of the Tokyo Round of multilateral trade negotiations (MTN), for which an agreement was signed in April 1979. Within the MTN, it had played a key role in the negotiation of the new Agreement on Subsidies and Countervailing Measures and took a special interest in encouraging developing countries to sign this agreement, as well as other codes of conduct on government procurement, import licensing, technical barriers to trade, antidumping, and customs valuation.

A permanent Declaration on Trade Policy by the members of the OECD was negotiated. Members pledged avoidance of protectionist action and declared their intention to facilitate positive adjustment to structural changes in world demand and production.

Treasury participated in interagency discussions on steel imports. Following those discussions and consultations with industry and foreign government officials, the administration suspended and then reinstated the trigger price mechanism for steel imports.

Treasury continued to play a leading role in the normalization of economic relations with the People's Republic of China. Over the past year, trade and banking relations have continued to expand very rapidly and agreements have been signed pertaining to textiles, civil aviation, maritime relations, consumer affairs, grain, and the Overseas Private Investment Corporation. The first formal meeting of the U.S.-China Joint Economic Committee was held in Washington in September 1980 under the chairmanship of Secretary Miller and Vice Premier Bo Yibo to review the entire range of bilateral economic issues, including especially business facilitation, trade expansion, finance, and investment.

In the sphere of export policy, the Treasury took a leading role in developing a legislative proposal to encourage the formation of export trading companies which would promote exports by small- and medium-sized firms. It also contributed to two studies mandated by Congress on U.S. competitiveness in international trade and on U.S. export promotion and disincentives. In the face of increasing export credit competition among exporting nations, Treasury officials continued to press negotiations to improve the International Arrangement on Export Credits, in order to reduce official export credit subsidies. Treasury also encouraged increased funding of the U.S. Export-Import Bank. Treasury assisted the Department of Agriculture in making a smooth transition from the use of direct Commodity Credit Corporation credits to guarantee programs, thereby encouraging greater participation by private financial entities in financing agricultural exports.

In the sphere of international investment, Assistant Secretary Bergsten chaired the Task Force on Private Foreign Investment which reported to the World Bank-IMF Development Committee. The report endorsed the objective of seeking an international understanding to limit the distorting effect of government investment incentives and recommended that the World Bank

group undertake a study of these incentive measures. The International Finance Corporation, an affiliate of the World Bank, is planning such a study.

### **Saudi Arabian Affairs**

In November 1979, the Secretary visited Saudi Arabia and signed a 5-year extension of the original United States-Saudi Arabian Technical Cooperation Agreement.

The United States-Saudi Arabian Joint Commission on Economic Cooperation met in Washington in April 1980, and reviewed 19 ongoing technical cooperation agreements. Plans for the future stress, even more than in the past, the training and development of Saudi Arabian professional and technical manpower. Projects include research in agriculture and water, desalination and solar energy, government statistics and administration, highways and transportation, and vocational training.

Arrangements were completed for the first United States-Saudi Arabian private sector dialogue to be held October 1-3, 1980, under the joint chairmanship of the Secretary and the Saudi Arabian Minister of Finance and National Economy.

### **International Economic Analysis**

Research studies on a number of subjects were completed, including (a) the role of State development agencies in U.S. adjustment to changing trade patterns, (b) the effect of "less than fair value" complaints and findings on U.S. import growth, 1975-79, (c) an empirical investigation of the effect of import penetration on domestic prices for U.S. manufactured goods, (d) an assessment of the competitive positions of U.S. industries, and (e) an appraisal of intervention practices in the foreign exchange market.

The task of processing, editing, and tabulating data from a survey of foreign portfolio investment in the United States as of December 31, 1978, was completed during the year. The survey had been required by the International Investment Survey Act of 1976. This act also requires a survey of U.S. portfolio investment abroad; a study of the need for, cost, and feasibility of surveying U.S. residents' portfolio abroad was submitted to Congress.





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## REVIEW OF TREASURY OPERATIONS

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## FINANCIAL OPERATIONS

### Summary

On the unified budget basis the deficit for fiscal 1980 was \$59.0 billion. Net receipts for fiscal 1980 amounted to \$520.1 billion (\$54.1 billion over fiscal 1979), and outlays totaled \$579.0 billion (\$85.4 billion over fiscal 1979).

Fiscal 1980 borrowing from the public amounted to \$70.5 billion as a result of (1) the \$59.0 billion deficit, (2) a \$0.4 billion increase in cash and monetary assets, and (3) an \$11.2 billion decrease in other means of financing.

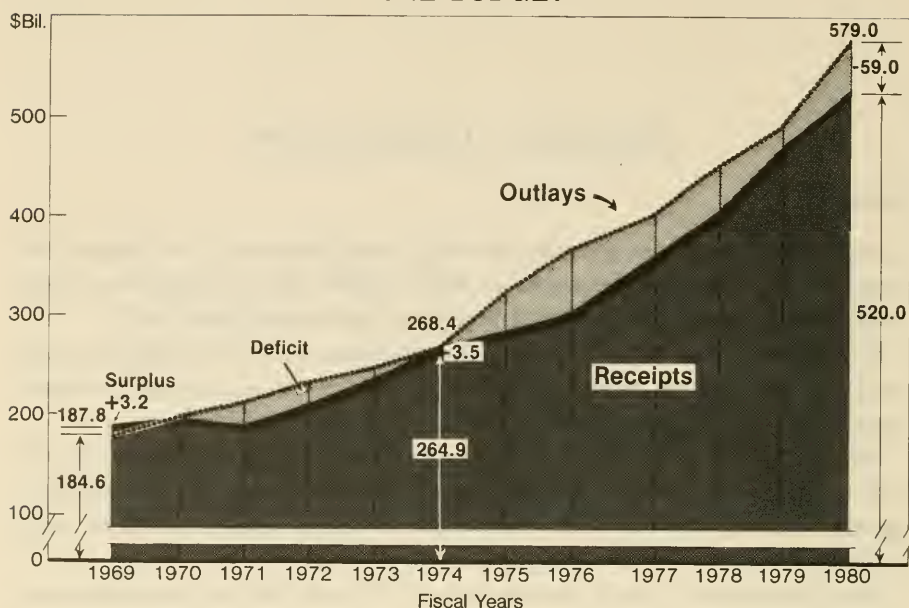
As of September 30, 1980, Federal securities outstanding totaled \$914.3 billion, comprised of \$907.7 billion in public debt securities and \$6.6 billion in agency securities. Of the \$914.3 billion, \$715.1 billion represented borrowing from the public.

The Government's fiscal operations for 1979 and 1980 are summarized as follows:

[In billions of dollars]

	1979	1980
Budget receipts and outlays:		
Receipts.....	466.0	520.1
Outlays.....	493.6	579.0
Budget deficit (-).....	-27.7	-59.0
Means of financing:		
Borrowing from the public (-).....	33.6	70.5
Increase in cash and other monetary assets.....	-.4	-.4
Other means:		
Increment on gold and seigniorage.....	1.0	.7
Profit on sale of gold.....	2.4	.9
Outlays of off-budget Federal agencies.....	-12.4	-14.2
Other .....	3.5	1.4
Total budget financing.....	27.7	59.0

## THE BUDGET



### Receipts

Total budget receipts amounted to \$520.1 billion in fiscal 1980, an increase of \$54.1 billion over fiscal 1979. Net budget receipts by major source for fiscal years 1979 and 1980 are shown below.

[In millions of dollars]

Source	1979	1980
Individual income taxes.....	217,841	244,069
Corporation income taxes.....	65,677	64,600
Employment taxes and contributions .....	120,074	138,765
Unemployment insurance .....	15,387	15,336
Contributions for other insurance and retirement .....	6,130	6,646
Excise taxes.....	18,745	24,329
Estate and gift taxes.....	5,411	6,389
Customs duties.....	7,439	7,174
Miscellaneous receipts.....	9,237	12,742
Total budget receipts.....	465,940	520,050

Projected estimates of receipts to future years, required of the Secretary of the Treasury, are shown and explained in the President's budget.

*Individual income taxes.*—Individual income taxes rose to \$244.1 billion in fiscal 1980, an increase of \$26.2 billion. The increase was due to the net effect of higher personal incomes and continued inflation that raised individuals to higher tax brackets offset somewhat by the tax reductions in the Revenue Act of 1978. While effective for calendar 1979, the full impact of the act was not reflected in receipts until fiscal 1980.

*Corporation income taxes.*—Corporation income taxes decreased \$1.1 billion from fiscal 1979 to fiscal 1980. This fall was due primarily to corporate profits in the first three quarters of 1980 being lower than in the comparable period for 1979. These lower profits resulted in lower estimated payments and higher tax refunds.

*Employment taxes and contributions.*—Receipts from this source totaled \$138.8 billion. This change of \$18.7 billion over the prior year reflected, in part, an increase in the social security taxable earnings base from \$22,900 to \$25,900, effective January 1, 1980.

*Unemployment insurance.*—Unemployment insurance receipts fell by \$0.1 billion in fiscal 1980. This occurred primarily because of a \$0.4 billion reduction in State tax deposits with the Treasury, the largest component of this category. State tax deposits dropped due to a lower average State tax rate which reflected increased State balances in the unemployment insurance trust fund.

*Contributions for other insurance and retirement.*—Receipts in this category increased by \$0.5 billion to a total of \$6.6 billion in fiscal 1980.

*Excise taxes.*—Receipts of excise taxes in fiscal 1980 were \$24.3 billion, an increase of \$5.6 billion over the prior year. This relatively large change is due primarily to amounts received for the windfall profit tax, which began April 1980. These receipts reflect continued phaseout of the telephone excise tax from 3 percent in 1979 to 2 percent in 1980.

*Estate and gift taxes.*—Receipts in this category increased by \$1.0 billion in fiscal 1980 to reach \$6.4 billion.

*Customs duties.*—Customs duties fell by \$0.3 billion in fiscal 1980 to \$7.2 billion.

*Miscellaneous receipts.*—These receipts totaled \$12.7 billion in fiscal 1980, an increase of \$3.5 billion. Deposits of earnings by the Federal Reserve System, the largest component of this category, increased by \$3.4 billion to reach \$11.8 billion. This large increase was due primarily to rising interest rates on Government securities.

## Outlays

Total outlays in fiscal 1980 were \$579.0 billion (compared with \$493.6 billion for 1979). Outlays by major agency for fiscal 1980 and the comparable prior period are presented in the following table. For details see the Statistical Appendix.

[In millions of dollars]

	1979	1980
Funds appropriated to the President.....	2,631	7,538
Agriculture Department .....	20,636	24,555
Defense Department .....	117,900	136,138
Education Department <sup>1</sup> .....	10,885	13,124
Energy Department .....	7,889	6,457
Environmental Protection Agency.....	4,800	5,602
Health and Human Services Department <sup>1</sup> .....	170,297	194,691
Housing and Urban Development Department.....	9,222	12,576
Labor Department .....	22,650	29,751
Transportation Department .....	15,486	18,963
Treasury Department .....	64,988	76,642
National Aeronautics and Space Administration .....	4,187	4,850
Veterans Administration .....	19,887	21,135
Other .....	40,640	49,485
Undistributed offsetting receipts .....	-18,488	-22,493
Total outlays.....	493,607	579,011

<sup>1</sup> Created May 4, 1980.**Cash and monetary assets**

On September 30, 1980, cash and monetary assets amounted to \$32.4 billion. The balance consisted of U.S. Treasury operating cash of \$21.0 billion (\$3.2 billion less than September 30, 1979); \$0.7 billion held in special drawing rights (\$0.2 billion less than September 30, 1979); a net \$1.4 billion with the International Monetary Fund (\$0.1 billion more than September 30, 1979); \$0.3 billion in loans to International Monetary Fund (\$0.3 more than September 30, 1979); and \$9.1 billion of other cash and monetary assets (\$3.3 billion more than September 30, 1979).

For a discussion of the assets and liabilities in the Treasury's account, see page 152. Transactions affecting the account in fiscal 1980 are shown in the following table:

*Transactions affecting the account of the U.S. Treasury, fiscal 1980*  
[In millions of dollars]

Operating balance Sept. 30, 1979 .....		24,176
Excess of deposits or withdrawals (-), budget, trust, and other accounts:		
Deposits .....	603,399	
Withdrawals (-).....	<u>650,296</u>	-46,897
Excess of deposits or withdrawals (-), public debt accounts:		
Increase in gross public debt .....		81,182
Deduct:		
Net discounts on new issues .....	21,711	
Interest increment on savings and retirement plan securities .....	4,203	
Net public debt transactions included in budget, trust, and other		
Government accounts .....	<u>11,551</u>	
Net deductions .....	<u>37,465</u>	43,717
Operating balance Sept. 30, 1980 .....		20,990

**Corporations and other business-type activities of the Federal Government**

The business-type programs which Government corporations and agencies administer are financed by appropriations (made available directly or in exchange for capital stock), borrowings from either the U.S. Treasury or the



public, or by revenues derived from their own operations. Various agencies have been borrowing from the Federal Financing Bank, which began operations in May 1974. The bank is authorized to purchase and sell securities issued, sold, or guaranteed by Federal agencies. Many Federal agencies finance programs through this bank that would otherwise involve the sale or issuance of credit market instruments, including agency securities, guaranteed obligations, participation agreements, and sales of assets.

Corporations or agencies having legislative authority to borrow from the Treasury issue their formal securities to the Secretary of the Treasury. Outstanding borrowings are reported as liabilities in the periodic financial statements of the Government corporations and agencies. In fiscal 1980 borrowings from the Treasury, exclusive of refinancing transactions, totaled \$147.2 billion, repayments were \$124.7 million, and outstanding loans on September 30, 1980, totaled \$128.8 billion.

Agencies having legislative authority to borrow from the public must consult with the Secretary of the Treasury regarding the proposed offering, or have the terms of the securities to be offered approved by the Secretary.

The Federal Financing Bank makes funds available in accordance with program requirements to agencies having authority to borrow from the bank and in recent years has become a major source of funds for these agencies. Interest rates shall not be less than rates determined by the Secretary of the Treasury taking into consideration current average yields on outstanding Government or bank securities of comparable maturity. The bank may charge fees to provide for expenses and reserves. During fiscal 1980, all funds loaned by the bank were borrowed from the Treasury.

During fiscal 1980, Congress granted new authority to borrow from the Treasury in the amount of \$20.1 billion, adjustments decreased borrowing authority by \$15.4 billion, making a total increase of \$4.7 billion. The status of borrowings and borrowing authority and the amount of corporation and agency securities outstanding as of September 30, 1980, are shown in the Statistical Appendix.

Unless otherwise specifically fixed by law, the Treasury determines interest rates on its loans to agencies by considering the Government's cost for its borrowings in the current market, as reflected by prevailing market yields on Government securities which have maturities comparable with the Treasury loans to the agencies. A description of the Federal agency securities held by the Treasury on September 30, 1980, is shown in the Statistical Appendix.

During fiscal 1980, the Treasury received \$9.5 billion from agencies which consisted of dividends, interest, and similar payments. (See the Statistical Appendix.)

As required by Department Circular No. 966, Revised, semiannual statements of financial condition, and income and retained earnings are submitted to the Treasury by Government corporations and business-type agencies (all other activities report on an annual basis). Quarterly statements showing direct and guaranteed loans, and annual statements of commitments

and contingencies are also submitted. These statements are the basis for the combined financial statements compiled by the Treasury which, together with individual statements, are published periodically in the Treasury Bulletin. Summary statements of the financial condition of Government corporations and other business-type activities, as of September 30, 1980, are shown in the Statistical Appendix.

Treasury Fiscal Requirements Manual Bulletin No. 79-10, issued under Transmittal Letter No. 274, dated August 3, 1979, advised agencies of an interim reporting requirement for factsheets and reports on the status of accounts and loans receivable. The required data, as of September 30, 1979, were submitted, and the reports were published in the July 1980 Treasury Bulletin. These two reports were not required as part of fiscal 1980 yearend reporting. A revised continuing reporting requirement on the status of agency receivables will be released by the U.S. Treasury later and will apply to fiscal 1981 receivables.

#### Joint Financial Management Improvement Program

During fiscal 1980, JFMIP continued to concentrate on studies and improvements in Government-wide financial management practices. An interagency study on the roles and responsibilities of certifying officers was completed, and a report of the findings and recommendations was released. A booklet of examples of good financial reports used by agency managers was also completed. Working with the Commerce Department and the Office of Personnel Management, JFMIP developed and pilot tested a productivity measurement system for accounting and finance offices. Another completed project was the issuance of a book on the "Early History of JFMIP."

On a continual basis, JFMIP has sponsored workshops and conferences and issued various publications to disseminate information on the current state of art in financial management improvements. Workshops on debt collection and productivity were held in Washington, D.C. The ninth annual Financial Management Conference, highlighting "A New Decade—The Outlook for Financial Management," was held on March 3, 1980.

Other projects initiated during 1980 include: (1) Compilation of description of various payroll and grant management systems within Federal agencies; (2) survey of several productivity measurement systems implemented in accounting and finance offices in Federal agencies; and (3) resolution of problems in the implementation of single audit concept.

## DOMESTIC FINANCE

### Federal Debt Management

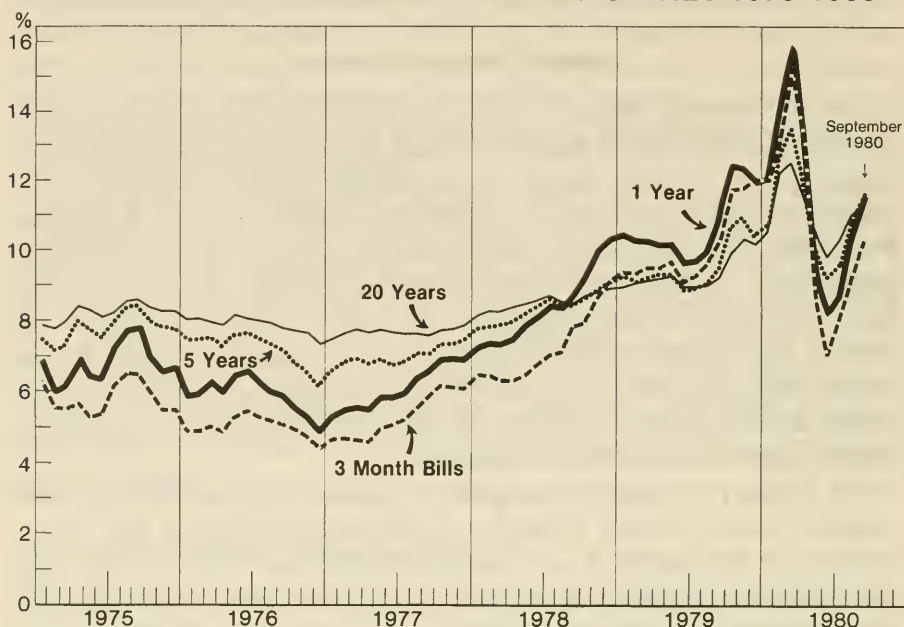
In fiscal 1980 the Treasury was required to refund record amounts of maturing securities and to finance a budget deficit of \$59 billion and an off-budget deficit of \$14.2 billion. These financings were conducted in an atmosphere of extraordinary uncertainty in financial markets. In October 1979 the Federal Reserve announced a major monetary policy shift toward greater focus on the money supply figures and less on interest rates. Both were extremely volatile throughout the year. Additional restraints on reserves and consumer credit controls were announced in March by the Federal Reserve. Inflation persisted throughout the year with interest rates setting alltime records. Pressures on the dollar in the foreign exchange markets were relieved as interest rates rose.

The Treasury continued its program of regular cycle note issues and debt extension, issuing 30-year bonds in the midquarter refundings and 15-year bonds in the first month of each quarter, although the Treasury's very large cash needs also required it to sell record amounts of bills. Despite the large amounts of coupon refunding and new money raised in the bill market, the Treasury was still able to accomplish further debt extension. By the end of the fiscal year the Treasury had increased the average length of the privately held marketable debt by 2 months to 3 years 9 months, thus contributing to a more balanced maturity structure of the debt and facilitating more efficient debt management in the future.

For the fiscal year, total Treasury marketable financing, excluding Treasury bills, amounted to \$135.5 billion of which \$85.3 billion was to refund maturing securities. Total new cash raised from marketable and nonmarketable issues amounted to \$71.1 billion for the fiscal year compared with \$35.6 billion in fiscal 1979, and \$63 billion in fiscal 1978. Heavy nonmarketable redemptions resulted in a net loss of \$12.5 billion, primarily due to savings bonds. Marketable securities, excluding the \$37 billion in cash management bills issued and redeemed during the fiscal year, provided \$38.3 billion from regular bills and \$45.3 billion from notes and bonds. The new cash raised from notes and bonds consisted of \$9.5 billion from 2-year cycle notes, \$4.7 billion from 4-year cycle notes, \$11.6 billion from 5-year cycle notes, \$6 billion from 15-year bonds, and \$3.2 billion from the 30-year long bonds; \$10.3 billion was raised in intermediate issues in the quarterly refundings.



## MARKET YIELDS AT CONSTANT MATURITIES 1975-1980<sup>1/</sup>



<sup>1/</sup>Monthly averages of daily market yields of public debt securities. Bank discount rates of Treasury bills.

### Changes in Federal securities

Federal securities include Treasury marketable and nonmarketable issues as well as those obligations issued by Federal agencies which are included in the unified budget totals and in which there is an element of Federal ownership. The Federal agency securities included are the participation certificates of the Government National Mortgage Association, the debt issues of the Export-Import Bank of the United States and the Tennessee Valley Authority, Postal Service bonds, Defense family housing mortgages, and various guaranteed debentures of the Federal Housing Administration.

At the close of fiscal 1980, there were \$914.3 billion of Federal securities outstanding, compared with \$833.8 billion a year earlier. Outstanding public debt issues of the Treasury amounted to \$907.7 billion, an increase of \$81 billion for the fiscal year. Outstanding Federal agency issues totaling \$6.6 billion were down \$0.6 billion from a year ago. Treasury marketable securities outstanding at the end of fiscal 1980 amounted to \$594.5 billion, an increase of \$87.8 billion for the year. Nonmarketable Treasury issues decreased by \$0.4 billion to a level of \$311.9 billion at the end of fiscal 1980. This decrease compares with an increase of \$30.5 billion in nonmarketable issues for fiscal 1979. Nearly 61 percent of the nonmarketables outstanding at the end of fiscal 1980 was in special nonmarketable issues only to Government accounts and trust funds. These issues increased \$13.5 billion in

*Federal debt and Government-sponsored agency debt*  
[In billions of dollars]

	Sept. 30, 1978	Sept. 30, 1979	Sept. 30, 1980	Increase or decrease
Public debt securities:				
Marketable public issues by maturity class:				
Within 1 year .....	225.4	246.7	276.5	29.8
1 to 5 years .....	168.5	157.3	195.8	38.5
5 to 20 years .....	65.9	71.7	88.8	17.1
Over 20 years .....	25.4	30.9	33.3	2.4
Total marketable issues .....	485.2	506.7	594.5	87.8
Nonmarketable public issues:				
Series E and H savings bonds .....	79.8	80.4	172.7	-7.7
U.S. savings notes <sup>2</sup> .....	.4	.4	.3	-.1
Investment series bonds .....	2.2	2.2	—	-2.2
Foreign government series:				
Dollar denominated .....	20.9	24.0	18.7	-5.2
Foreign currency denominated .....	.8	4.2	6.4	2.3
State and local government series .....	24.2	24.6	23.6	-.9
Other nonmarketable debt .....	.1	.1	.1	(*)
Total nonmarketable public issues .....	128.4	136.0	122.0	-13.9
Government account series (nonmarketable) .....	153.3	176.3	189.8	13.5
Non-interest-bearing debt .....	4.6	7.5	1.3	-6.2
Total gross public debt .....	771.5	826.5	907.7	81.2
Federal agency securities:				
Gov't National Mortgage Association .....	3.2	3.0	2.8	-.2
Export-Import Bank of the United States .....	2.1	.9	.7	-.2
Tennessee Valley Authority .....	1.8	1.7	1.7	—
Defense family housing .....	.9	.8	.6	-.2
Other .....	.9	.8	.8	—
Total Federal agency debt .....	8.9	7.2	6.6	-.6
Total Federal debt .....	780.4	833.8	914.3	80.6
Government-sponsored agency securities:				
Federal home loan banks .....	27.4	45.5	54.1	8.6
Federal National Mortgage Association .....	38.4	46.1	51.7	5.6
Federal land banks .....	20.2	17.1	12.8	-4.3
Federal intermediate credit banks .....	11.6	2.7	1.8	-.9
Banks for cooperatives .....	4.3	.8	.6	-.2
Farm Credit discount notes .....	2.8	3.4	3.4	—
Farm Credit consolidated bonds .....	2.3	25.9	42.6	16.7
Government-sponsored agency debt .....	107.0	141.4	166.9	25.5

<sup>1</sup> Revised.

\* Less than \$50 million.

<sup>1</sup> Includes series EE and HH which replaced series E and H, effective Jan. 1, 1980.

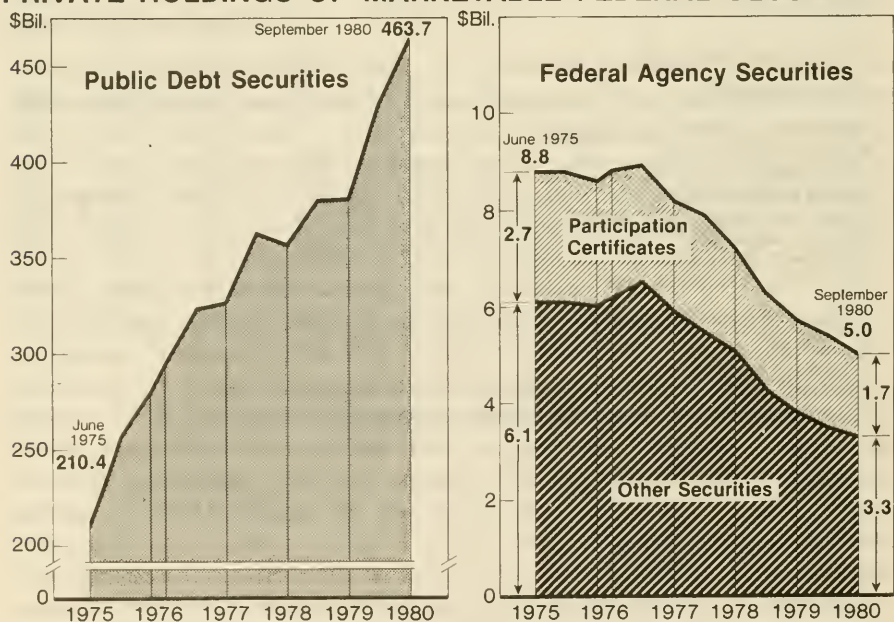
<sup>2</sup> U.S. savings notes first offered in May 1967; sales discontinued after June 30, 1970.



fiscal 1980, compared with an increase of \$23.1 billion in fiscal 1979. Special nonmarketable issues to foreign official accounts decreased \$3 billion in fiscal 1980; this compares with a \$6.4 billion increase in these issues in fiscal 1979. In addition, special nonmarketable issues to State and local governments decreased in fiscal 1980 by \$0.9 billion, compared with an increase of \$0.3 billion in fiscal 1979. The decrease in savings bonds in fiscal 1980 of \$7.7 billion compares with a small increase of \$0.6 billion in fiscal 1979. In addition, the Investment Series B bonds which had been outstanding in the amount of \$2.2 billion at the end of fiscal 1979 matured during 1980 and were not replaced.

Federal securities do not include the securities issued by Government-sponsored agencies since these agencies are not owned in whole or in part by the Government, although they are subject to some degree of Federal supervision. In fiscal 1980, the debt of Government-sponsored agencies increased by \$25.5 billion to a level of \$166.9 billion. The Farm Credit System's consolidated bonds and discount notes increased by \$16.7 billion and the issues of the Federal home loan banks rose \$8.6 billion. Securities issued by the Federal National Mortgage Association increased \$5.6 billion, while outstanding issues of the Federal intermediate credit banks declined \$0.9 billion. Banks for cooperatives issues fell \$0.2 billion and Federal land bank issues decreased \$4.3 billion. At the end of fiscal 1980 private investors held \$159.1 billion of Government-sponsored agency securities.

## PRIVATE HOLDINGS OF MARKETABLE FEDERAL SECURITIES



*Estimated ownership of public debt securities on selected dates 1978-80*  
 [Dollar amounts in billions]

	Sept. 30, 1978	Sept. 30, 1979	Sept. 30, 1980	Change during fiscal 1980
Estimated ownership by:				
Private nonbank investors:				
Individuals: <sup>1</sup>				
Series E and H savings bonds .....	\$79.5	\$80.4	<sup>2</sup> \$72.7	-\$7.7
U.S. savings notes <sup>3</sup> .....	.4	.4	.3	-.1
Other securities .....	<sup>†</sup> 33.1	<sup>†</sup> 34.7	50.0	15.3
Total individuals .....	<sup>†</sup> 113.0	<sup>†</sup> 115.5	123.0	7.5
Insurance companies .....	15.1	<sup>†</sup> 14.9	14.4	-.5
Mutual savings banks .....	5.2	<sup>†</sup> 4.8	5.3	.5
Savings and loan associations .....	8.3	<sup>†</sup> 6.3	8.6	2.3
State and local governments .....	<sup>†</sup> 63.8	<sup>†</sup> 67.1	73.4	6.3
Foreign and international .....	120.0	125.2	126.0	.8
Corporations .....	<sup>†</sup> 19.4	<sup>†</sup> 24.0	25.0	1.5
Miscellaneous investors <sup>4</sup> .....	<sup>†</sup> 48.1	<sup>†</sup> 75.4	112.2	36.8
Total private nonbank investors .....	<sup>†</sup> 393.8	<sup>†</sup> 433.2	488.4	55.2
Commercial banks .....	<sup>†</sup> 94.4	<sup>†</sup> 90.1	100.9	10.8
Federal Reserve banks .....	115.3	115.5	120.7	5.2
Government accounts .....	168.0	187.7	197.7	10.0
Total gross debt outstanding .....	771.5	826.5	907.7	81.2
Percent owned by:				
Individuals .....	15	14	14	
Foreign and international .....	16	15	14	
Other private nonbank investors .....	20	23	26	
Commercial banks .....	12	11	11	
Federal Reserve banks .....	15	14	13	
Government accounts .....	22	23	22	
Total gross debt outstanding .....	100	100	100	

<sup>†</sup>Revised.

<sup>1</sup>Including partnerships and personal trust accounts.

<sup>2</sup>Includes series EE and HH which replaced series E and H, effective Jan. 1, 1980.

<sup>3</sup>U.S. savings notes first offered in May 1967; sales discontinued after June 30, 1970.

<sup>4</sup>Includes nonprofit institutions, corporate pension trust funds, nonbank Government security dealers, certain Government deposit accounts, Government-sponsored agencies, and other investor groups not shown above.

### Estimated ownership

Private investors held \$589.2 billion of the \$907.7 billion total of Federal securities outstanding at the end of fiscal 1980. Federal Reserve banks and Government accounts held the remaining \$318.5 billion. Borrowing from the public, which includes the Federal Reserve as well as private investors, amounted to a net \$70.5 billion, compared with \$33.6 billion in fiscal 1979. Private investors, including foreign and international investors, accounted for an increase in Federal securities of \$65.3 billion.

*Individuals.*—Holdings of public debt securities by individuals increased \$7.5 billion in fiscal 1980, compared with a small increase of \$2.5 billion in fiscal 1979. The decrease of \$7.7 billion in savings bonds was due to the unprecedented excess redemptions over sales because of the relatively low

interest rate on savings bonds compared with record high market rates of interest. Holdings of other Treasury securities increased by \$15.2 billion. At the end of fiscal 1980, individuals held \$123 billion of public debt securities, of which \$73 billion were savings bonds and notes. Holdings of Federal agency securities amounting to \$0.4 billion were about the same as at the end of fiscal 1979.

*Insurance companies.*—Public debt securities held by insurance companies declined \$0.5 billion in fiscal 1980; this compares with a comparable decline of \$0.2 billion in fiscal 1979. At the end of fiscal 1980, insurance companies held \$14.4 billion of public debt securities and \$0.6 billion of Federal agency securities.

*Savings and loan associations.*—Savings and loan associations increased their holdings of public debt securities in fiscal 1980 by \$2.3 billion, compared with a decrease of \$2 billion in fiscal 1979. Holdings at the end of the fiscal year amounted to \$8.6 billion of public debt issues and \$0.6 billion of Federal agency securities.

*Mutual savings banks.*—Mutual savings banks also increased their holdings of public debt securities in fiscal 1980. This increase of \$0.5 billion compares with a decrease of \$0.4 billion in fiscal 1979. Their holdings of Federal agency securities declined to \$0.5 billion at the end of the fiscal year. Their holdings of public debt securities at the end of fiscal 1980 were \$5.3 billion.

*State and local governments.*—Public debt securities held by State and local governments at the end of fiscal 1980 amounted to \$73.4 billion, up \$6.3 billion from their holdings of marketable securities at the end of fiscal 1979. Special nonmarketable issues to State and local governments declined by \$0.9 billion in fiscal 1980; this compares with a smaller decline of \$0.3 billion in fiscal 1979.

*Foreign and international.*—Foreign investors increased their holdings of public debt securities in fiscal 1980 by \$0.8 billion. Special nonmarketables decreased in fiscal 1980 by \$2.9 billion to \$25.1 billion. Foreign-currency-denominated issues increased to \$6.4 billion. This increase consisted of \$2.3 billion of issues denominated in deutsche marks. Federal agency securities held by foreign and international investors declined by \$0.2 billion at the end of fiscal 1980.

*Nonfinancial corporations.*—Corporations increased their holdings of public debt securities \$1.5 billion, down from the \$2.4 billion increase in fiscal 1979. At the end of September 1980 they held \$25.5 billion of public debt securities. Holdings of Federal agency issues declined \$0.3 billion for the year.

*Other private nonbank investors.*—Public debt holdings of other private nonbank investors increased by \$27.9 billion in fiscal 1980, somewhat less than the nearly \$31 billion increase in fiscal 1979. Holdings of Federal agencies securities declined \$0.2 billion.

*Commercial banks.*—At the end of fiscal 1980 banks held \$100.9 billion of public debt securities, an increase of \$10.8 billion from their holdings in fiscal 1979. Holdings of Federal agency issues declined very slightly to \$0.9 billion.

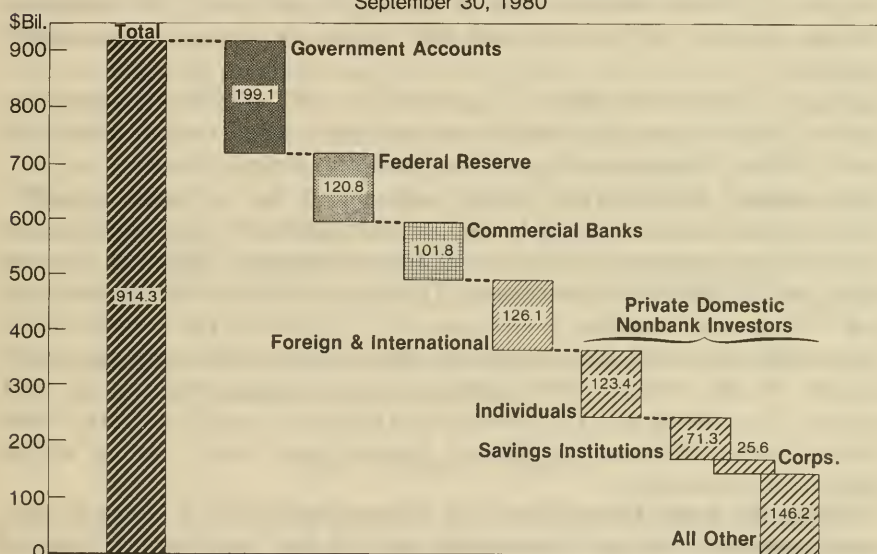


**Federal Reserve System.**—The Federal Reserve System's holdings of public debt securities increased by \$5.2 billion. This contrasts with the increase of just \$0.2 billion in fiscal 1979. At the end of fiscal 1980 the System held \$120.7 billion of public debt securities and \$0.1 billion of Federal agency securities.

**Government accounts.**—Public debt securities held by Government accounts increased by \$10 billion in fiscal 1980, compared with an increase of \$19.7 billion in fiscal 1979 and \$12.5 billion in fiscal 1978. Holdings of special nonmarketable issues increased by \$13.5 billion to \$189.8 billion. Federal agency security holdings fell by \$0.1 billion to \$1.4 billion at the end of fiscal 1980. Holdings of public debt securities at the end of the fiscal year amounted to \$197.7 billion.

## OWNERSHIP OF FEDERAL SECURITIES

September 30, 1980



### Market financing operations

Treasury began the fiscal year with two auctions of a 2-year note and a 4-year note for issue October 9 and 10. These auctions had been postponed from their scheduled September dates because Congress delayed action on the temporary debt limit legislation. Regular 2-year and 4-year cycle notes continued to be offered throughout fiscal 1980 as they had in the past. In addition, the Treasury made regular quarterly sales of 5-year notes and 15-year bonds to raise new cash. The 15-year bonds were issued during the first month of each calendar quarter in the amount of \$15 billion. The 5-year notes were issued in the last month of each quarter in amounts varying from \$2.5 to

\$3 billion. Each of the offerings of the 5-year notes attracted foreign investors, thus increasing the size of the issue.

Quarterly refundings remained an important part of the total financing operations of the Treasury in fiscal 1980. The first of these, announced October 24, 1979, was the sale of \$2.8 billion of 3½-year notes, \$2 billion of 10-year notes, and \$2 billion of 30-year bonds to refund \$5.4 billion of maturing securities and to raise about \$1.4 billion of new cash. The sale of the 3½-year notes brought a record average return of 11.64 percent. The 10-year note sale at 10.75 percent and the 30-year bond at 10.44 percent were also records although none of the auctions attracted much investor interest.

In November of 1979 the Treasury sold additional foreign-currency-denominated notes for 2 billion deutsche marks, consisting of \$451 million in 2½-year notes at 8.5 percent and \$668 million in 3½-year notes at 8.55 percent. DM issues were also sold in January in amounts of \$561 million in 2½-year notes at 8.50 percent and \$607 million in 3½-year notes at 8.45 percent.

On the 15-year bond sold early in January the yield of 10.6 percent was the highest yield ever for this maturity and the highest on a Treasury bond since the Civil War. Subsequent 15-year bond issue sales also set records.

On January 30, 1980, the Treasury announced that it would raise \$2.6 billion in new cash and refund \$4.7 billion in maturing securities by selling in its midquarter refunding \$3.3 billion of 3½-year notes, \$2 billion of 7¼-year notes, and \$2 billion of 30-year bonds. The average yield on the 3½-year note was 11.98 percent resulting in a coupon of 11⅞ percent. The coupon on the intermediate issue was set at 12 percent, the average yield having been 12.02 percent. In the 30-year bond auction a record average was set at 11.84 percent. The coupon was 11¾ percent, the highest ever for a security of that length. During February and March interest rates soared, setting alltime highs for all maturities.

During the April-June quarter, the Treasury issued \$15.8 billion in cash management bills. These as well as the \$18.2 billion issued in the first two quarters of the fiscal year were all retired as they came due in this quarter. The unusually heavy cash demands throughout the January-June period were due largely to the large redemptions of savings bonds and redemptions by foreign investors of Treasury nonmarketables to raise dollars. An increase in the savings bond interest rate, from 6½ percent to 7 percent, in January, on the new series EE bonds, had no perceptible impact on the cash drain. Treasury requested repeal of the savings bond interest rate ceiling, but Congress did not complete action on this request in fiscal 1980.

On April 30, 1980, the Treasury announced its plans to raise net new cash of \$3.5 billion by selling in its midquarter refunding \$3.5 billion of 3¼-year notes, \$2 billion of 9½-year notes, and \$2 billion of 30-year bonds. The 9½-year notes were a reopening of the 10¾ percent 10-year notes originally issued November 15, 1979, and were thus sold at a price auction. The resulting average price was 105.27 with an approximate yield of 9.88 percent.



A foreign add-on of \$55 million increased the size of the issue. The short note sale resulted in an average yield of 9.32 percent. The coupon was  $9\frac{1}{4}$  percent. In the bond auction the average yield was 10.12 percent for a coupon of 10 percent.

In late May the Treasury was forced to delay the auction of both the 2-year note and the 5-year  $2\frac{1}{2}$ -month note as Congress had not yet acted on the legislation to raise the temporary debt limit. The \$879 billion temporary debt limit was extended May 30, 1980, to June 5, 1980, and for the first time in history, the Treasury on May 30, 1980, announced, auctioned, and issued a security on the same day. This sale was a cash management bill of \$2 billion. The act of June 6, 1980, extended the then-current limit to June 30, 1980. Congress acted on June 28 to increase the temporary debt limit to \$925 billion through February 28, 1981, thus allowing normal financing operations to continue.

The August quarterly financing, announced on July 30, 1980, refunded \$5 billion of maturing securities and raised \$3.2 billion of new cash. Three issues were offered: \$4 billion of  $3\frac{1}{4}$ -year notes, \$2.8 billion of 10-year notes, and \$1.5 billion of  $29\frac{1}{4}$ -year bonds. The  $29\frac{1}{4}$ -year bonds were an addition to the  $10\frac{3}{8}$  percent bonds of 2004–2009 originally issued November 15, 1979.

The reopening of the  $10\frac{3}{8}$  percent bond for \$1.5 billion exhausted the Treasury's existing \$50 billion authority to issue securities maturing in more than 10 years with coupons greater than  $4\frac{1}{4}$  percent. On September 29, 1980, Congress passed a bill to increase this amount to \$70 billion effective October 1, 1980.

For allotments by investor class of marketable Treasury securities for fiscal 1980, see table 36 in the Statistical Appendix.

### State and Local Finance

The Deputy Assistant Secretary for State and Local Finance is responsible for the Offices of New York Finance, Urban and Regional Economics, State-Local Fiscal Research and Evaluation, and Municipal Finance. The overall mission of these offices includes: Policy development for general-purpose fiscal assistance such as revenue sharing and countercyclical aid; assessing the impacts of Federal aid on State and local governments; monitoring State-local fiscal trends and access to the tax-exempt market, including specifically the situation in New York City; advising the Secretary of the Treasury concerning Federal responses to State and local fiscal problems and the role of general assistance in economic stabilization policy; and representing the Department of the Treasury before public interest groups and Congress on intergovernmental fiscal matters.

In addition, the Deputy Assistant Secretary has policy responsibility for the Office of Revenue Sharing, a separate agency within Treasury. This responsibility was especially important in fiscal 1980, when proposals for the reauthorization of the revenue sharing program were developed and

*Offerings of marketable Treasury securities excluding refunding of regular bills, fiscal 1980*  
 [In millions of dollars]

Date	Description	Allotted to private investors		Allotted to Federal Reserve and Government accounts	Total	Average auction yield (percent)
		For cash	For refunding			
NOTES AND BONDS						
1979						
Oct. 9 .... 10%	percent note, Sept. 30, 1981.....	-166	3,461	400	3,695	10.21
Oct. 10 .... 9%	percent note, Sept. 30, 1983.....	721	1,813	268	2,802	9.79
Oct. 18 .... 10%	percent bond, Nov. 15, 1994.....	1,502	.....	.....	1,502	10.17
Oct. 31 .... 12%	percent note, Oct. 31, 1981.....	123	3,864	470	4,457	12.66
Nov. 15 .... 11%	percent note, May 15, 1983.....	667	2,151	800	3,618	11.64
Nov. 15 .... 10%	percent note, Nov. 15, 1989.....	416	1,601	400	2,417	10.75
Nov. 15 .... 10%	percent bond, Nov. 15, 2004-09..	365	1,638	314	2,317	10.44
Nov. 30 .... 12%	percent note, Nov. 30, 1981.....	103	4,289	502	4,894	12.24
Dec. 4 .... 10%	percent note, May 15, 1985.....	2,539	.....	.....	2,539	10.40
Dec. 31 .... 11%	percent note, Dec. 31, 1981.....	387	3,349	571	4,307	11.43
Dec. 31 .... 10½	percent note, Dec. 31, 1983.....	695	1,850	156	2,701	10.52
1980						
Jan. 10 .... 10½	percent bond, Feb. 15, 1995.....	1,502	.....	.....	1,502	10.60
Jan. 31 ... 11½	percent note, Jan. 31, 1982.....	610	3,472	403	4,485	11.52
Feb. 15 .... 11%	percent note, Aug. 15, 1983.....	1,222	2,085	978	4,285	11.98
Feb. 15 .... 12	percent note, May 15, 1987.....	738	1,284	450	2,472	12.02
Feb. 15 .... 11%	percent note, Feb. 15, 2005-10...	718	1,285	644	2,647	11.84
Feb. 29 ... 13%	percent note, Feb. 28, 1982.....	678	3,421	399	4,498	13.98
Mar. 3 .... 14%	percent note, May 15, 1985.....	2,719	.....	.....	2,719	14.39
Mar. 31 ... 15	percent note, Mar. 31, 1982.....	374	3,198	500	4,072	15.01
Mar. 31 ... 14½	percent note, Mar. 31, 1984.....	536	2,069	309	2,914	14.29
Apr. 8 .... 12%	percent bond, May 15, 1995.....	1,503	.....	.....	1,503	12.69
Apr. 30 ... 11%	percent note, Apr. 30, 1982.....	1,393	2,721	459	4,573	11.44
May 15 ... 9%	percent note, Aug. 15, 1983.....	2,882	788	3,000	6,670	9.32
May 15 ... 10%	percent note, Nov. 15, 1989.....	1,600	462	1,300	3,362	9.88
May 15 ... 10	percent bond, May 15, 2005-10...	1,549	462	975	2,986	10.12
June 4 .... 9%	percent note, May 31, 1982.....	1,186	2,824	274	4,284	9.37
June 5 .... 9%	percent note, Aug. 15, 1985.....	3,293	.....	.....	3,293	9.66
June 30 ... 8%	percent note, June 30, 1982.....	824	3,691	700	5,215	8.63
June 30 ... 8%	percent note, June 30, 1984.....	1,525	1,697	505	3,727	8.99
July 9 .... 10%	percent bond, May 15, 1995.....	1,504	.....	.....	1,504	10.42
July 31 ... 8%	percent note, July 31, 1982.....	1,212	3,337	788	5,337	8.97
Aug. 15 ... 9%	percent note, Nov. 15, 1983.....	1,609	2,473	1,750	5,832	9.88
Aug. 15 ... 10%	percent note, Aug. 15, 1990.....	1,097	1,665	1,000	3,762	10.81
Aug. 15 ... 10%	percent bond, Nov. 15, 2004-09..	592	908	384	1,884	10.71
Sept. 2 .... 11%	percent note, Aug. 31, 1982.....	1,582	2,975	570	5,127	11.24
Sept. 3 ... 11%	percent note, Nov. 15, 1985.....	3,087	.....	.....	3,087	11.76
Sept. 30 ... 11%	percent note, Sept. 30, 1982.....	1,214	3,356	550	5,120	11.93
Sept. 30 ... 12½	percent note, Sept. 30, 1984.....	1,228	1,802	339	3,369	12.13
Total notes and bonds.....		45,329	69,991	20,158	135,478	....

considered by the Senate Finance Committee and the House Government Operations Committee.<sup>1</sup> Both committees reported bills in September.

The Deputy Assistant Secretary also serves as the Department's principal or deputy liaison with several interagency groups responsible for coordination of policies and programs relating to State, local, and territorial governments. These include the Statistical Policy Coordination Committee, the Committee on Interagency Territorial Assistance, and the Interagency Coordinating Council. The latter was established as a key element of the

<sup>1</sup> See exhibit 22.

*Offerings of marketable Treasury securities excluding refunding of regular bills,  
fiscal 1980—Continued*

Date	Description	Allotted to private investors		Allotted to Federal Reserve and Government accounts	Total	Average auction yield (percent)
		For cash	For refunding			
BILLS (MATURITY VALUE)						
Change in offerings of regular bills:						
1979	October–December.....	3,876	.....	.....	3,876	.....
1980	January–March.....	7,165	.....	.....	7,165	.....
	April–June.....	12,142	.....	.....	12,142	.....
	July–September.....	15,151	.....	.....	15,151	.....
	Total change in regular bills.....	38,334	.....	.....	38,334	.....
Other bill offerings:						
1979						
Nov. 9.....	12.583 percent 167-day, maturing					
	Apr. 24, 1980.....	2,004	.....	.....	2,004	.....
Dec. 3.....	11.646 percent 143-day, maturing					
	Apr. 24, 1980.....	3,001	.....	.....	3,001	.....
Dec. 10.....	11.738 percent 157-day, maturing					
	May 15, 1980.....	2,326	.....	.....	2,326	.....
1980						
Mar. 5.....	15.296 percent 43-day, maturing					
	Apr. 17, 1980.....	4,001	.....	.....	4,001	.....
Mar. 25.....	16.122 percent 37-day, maturing					
	May 1, 1980.....	6,904	.....	.....	6,904	.....
Apr. 3.....	16.855 percent 77-day, maturing					
	June 19, 1980.....	5,041	.....	.....	5,041	.....
Apr. 7.....	15.714 percent 80-day, maturing					
	June 26, 1980.....	4,031	.....	.....	4,031	.....
May 29.....	8.072 percent 19-day, maturing					
	June 17, 1980.....	2,702	.....	.....	2,702	.....
May 30.....	9.720 percent 13-day, maturing					
	June 12, 1980.....	2,001	.....	.....	2,001	.....
June 3.....	10.260 percent 2-day, maturing					
	June 5, 1980.....	2,002	.....	.....	2,002	.....
Aug. 4.....	8.498 percent 43-day, maturing					
	Sept. 16, 1980.....	3,004	.....	.....	3,004	.....
	Total other bill offerings.....	37,017	.....	.....	37,017	.....
	Total offerings.....	120,680	69,991	20,158	210,829	.....

President's urban policy announced in March 1978. The Office also deals with State and local governments directly and through their interest groups in Washington.

#### Office of New York Finance

During fiscal 1980, the Office of New York Finance exercised the Department's oversight responsibilities pursuant to the provisions of the New York City Loan Guarantee Act of 1978 (Public Law 95-339).<sup>2</sup> This act authorizes the Secretary to extend up to \$1.65 billion in Federal guarantees of city debt through June 30, 1982, when the act expires.

<sup>2</sup> See exhibit 20.

*Disposition of marketable Treasury securities excluding regular bills, fiscal 1980<sup>1</sup>*  
[In millions of dollars]

Date of retirement	Securities		Redeemed for cash or carried to matured debt	Exchanged for new issue at maturity	Total
	Description and maturing date	Issue date			
1979					
NOTES AND BONDS					
Oct. 1 .....	1½ percent note, Oct. 1, 1979 .....	Oct. 1, 1974 .....	1	.....	1
Oct. 31 .....	7¼ percent note, Oct. 31, 1979 .....	Oct. 31, 1977 .....	3,864	470	4,334
Nov. 15 .....	6¼ percent note, Nov. 15, 1979 .....	Nov. 15, 1976 .....	3,125	251	3,376
Nov. 15 .....	7 percent note, Nov. 15, 1979 .....	Nov. 15, 1973 .....	1,873	368	2,241
Nov. 15 .....	6½ percent note, Nov. 15, 1979 .....	Feb. 15, 1973 .....	709	895	1,604
Nov. 30 .....	7½ percent note, Nov. 30, 1979 .....	Nov. 30, 1976 .....	4,289	502	4,791
Dec. 31 .....	7½ percent note, Dec. 31, 1979 .....	Jan. 3, 1978 .....	3,349	571	3,920
Dec. 31 .....	7½ percent note, Dec. 31, 1979 .....	Jan. 6, 1976 .....	1,850	156	2,006
1980					
Jan. 31 .....	7½ percent note, Jan. 31, 1980 .....	Jan. 31, 1978 .....	3,472	403	3,875
Feb. 15 .....	6½ percent note, Feb. 15, 1980 .....	Feb. 15, 1977 .....	3,096	1,512	4,608
Feb. 15 .....	4 percent bond, Feb. 15, 1980 .....	Jan. 23, 1959 .....	2,079	266	2,345
Feb. 29 .....	7½ percent note, Feb. 29, 1980 .....	Feb. 28, 1978 .....	3,421	399	3,820
Mar. 31 .....	7½ percent note, Feb. 29, 1980 .....	Mar. 17, 1976 .....	5,267	809	6,076
Apr. 1 .....	1½ percent note, Apr. 1, 1980 .....	Apr. 1, 1975 .....	2	.....	2
Apr. 30 .....	7¼ percent note, Apr. 30, 1980 .....	Apr. 30, 1980 .....	2,721	459	3,180
May 15 .....	6½ percent note, May 15, 1980 .....	May 15, 1973 .....	1,712	5,553	7,265
May 31 .....	8 percent note, May 31, 1980 .....	May 31, 1978 .....	2,824	274	3,098
June 30 .....	8¾ percent note, June 30, 1980 .....	May 30, 1978 .....	3,707	700	4,407
June 30 .....	7½ percent note, June 30, 1980 .....	June 10, 1976 .....	1,680	505	2,185
July 31 .....	8½ percent note, July 31, 1980 .....	July 31, 1978 .....	3,337	827	4,164
Aug. 15 .....	6½ percent note, Aug. 15, 1980 .....	Aug. 15, 1977 .....	3,435	698	4,133
Aug. 15 .....	9 percent note, Aug. 15, 1980 .....	Aug. 15, 1974 .....	1,860	2,436	4,296
Aug. 31 .....	8½ percent note, Aug. 31, 1980 .....	Aug. 31, 1978 .....	2,975	570	3,545
Sept. 30 .....	8½ percent note, Sept. 30, 1980 .....	Oct. 2, 1978 .....	3,356	550	3,906
Sept. 30 .....	6½ percent note, Sept. 30, 1980 .....	Sept. 14, 1976 .....	1,802	339	2,141
Total coupon securities.....			65,806	19,513	85,319
1980					
BILLS					
Other:					
Apr. 17 .....	15.296 percent (43-day).....	Mar. 5, 1980 .....	4,001	.....	4,001
Apr. 24 .....	12.583 percent (167-day).....	Nov. 9, 1979 .....	2,004	.....	2,004
Apr. 24 .....	11.646 percent (143-day).....	Dec. 3, 1979 .....	3,001	.....	3,001
May 1 .....	16.122 percent (37-day).....	Mar. 25, 1980 .....	6,904	.....	6,904
May 15 .....	11.738 percent (157-day).....	Dec. 10, 1979 .....	2,326	.....	2,326
June 5 .....	10.260 percent (2-day).....	June 3, 1980 .....	2,002	.....	2,002
June 12 .....	9.720 percent (13-day).....	May 30, 1980 .....	2,001	.....	2,001
June 17 .....	8.072 percent (19-day).....	May 29, 1980 .....	2,702	.....	2,702
June 19 .....	16.855 percent (77-day).....	Apr. 3, 1980 .....	5,041	.....	5,041
June 26 .....	15.714 percent (80-day).....	Apr. 7, 1980 .....	4,031	.....	4,031
Sept. 16 .....	8.498 percent (43-day).....	Aug. 4, 1980 .....	3,004	.....	3,004
Total other bills.....			37,017	.....	37,017
Total securities .....			102,823	19,513	122,336

<sup>1</sup>Excludes \$5.9 billion of notes which matured Sept. 30, 1979, but were not refunded until Oct. 9 and 10, 1979, as shown in the preceding "Offerings" table, because of delayed action on the debt limit legislation.

During this period, New York City is required to achieve a balanced budget in accordance with generally accepted accounting principles and to implement other budget and financial reforms. These actions are designed to enable the city to regain access to conventional borrowing sources so that, in collaboration with the Municipal Assistance Corporation, it will be able to



meet its short- and long-term financing needs in the public credit markets after June 30, 1982.

Under the terms of Public Law 95-339, the Secretary of the Treasury may extend guarantees only if, among other things, there is a reasonable prospect of repayment of the city indebtedness, the city is unable to obtain credit on reasonable terms in the public markets or elsewhere in amounts sufficient to meet its financing needs, and the city is making substantial progress toward a balanced budget in accordance with generally accepted accounting principles in its fiscal 1982.

In fiscal 1980, the Secretary determined that New York City was in compliance with the conditions set forth in the act, and \$250 million in guarantees were extended. For example, the Secretary determined that the city had made substantial progress toward a balanced budget in its fiscal 1982. In fact the city plans to balance the budget for its fiscal 1981, 1 year earlier than the statutory requirement.

#### **Office of Municipal Finance**

The Office of Municipal Finance continued in its duties to review developments and proposals relating to debt finance and the financial administration of State and local governments. The Office gives particular attention to State-local budgetary and accounting practices. In addition, the Office reviews the impacts of tax and expenditure limitations on State and local government finance.

The Office is responsible for monitoring current issues affecting the municipal credit market. These include governmental accounting principles, disclosure practices relating to the sale of State and local securities, and the proliferation of mortgage-subsidy and industrial-development bonds in the tax-exempt market.

#### **Office of State and Local Fiscal Research and Evaluation**

The major activity of the Office of State and Local Fiscal Research and Evaluation in fiscal 1980 involved preparation of a study of the effects on revenue sharing payments through 1985 of extraordinary increases in the prices of domestically produced energy (coal, crude oil, and natural gas). The results of the study provided evidence relating to the desirability of changing the extent to which severance taxes are included in the tax effort calculation in the formula by which revenue sharing payments are allocated among the States.

The Office continued to monitor congressional efforts to enact countercyclical fiscal assistance legislation. In March 1980, the administration withdrew support for any countercyclical legislation and eliminated countercyclical funds from the 1981 budget because of the necessity for additional budgetary restraint to help fight inflation. In August and September, because of changed economic circumstances and renewed congressional interest, the administra-



tion worked to assist Congress in the design of a countercyclical title to be included in the reauthorization of revenue sharing.

The Office monitors actual developments and forecasts of the overall fiscal position of State and local governments in the national economy. Ad hoc assessments were prepared on numerous occasions.

The Office also provided technical support for the administration's efforts to enact a targeted fiscal assistance program to provide general assistance to fiscally stressed local governments. Bills for fiscal 1980 incorporating such a program were approved by both Houses but died in the absence of a conference.

The capacity of the Office to carry on research and evaluation was strengthened in 1980 by improving its direct access to computer models and data bases. This capacity is also used by the Office of Urban and Regional Economics and the Office of Municipal Finance.

#### **Office of Urban and Regional Economics**

The Office of Urban and Regional Economics is responsible for evaluating local and regional economic trends and their impacts on the fiscal condition of State and local governments. In addition, it assesses the impacts of specific Federal economic policies on local economies.

In fiscal 1980, the Office continued to participate in the White House Task Force on Small Communities and Rural Development to coordinate and enhance programs to assist the economic development and financial stability of small communities and rural areas.

In preparation for congressional consideration of the renewal of revenue sharing, the Office was responsible for monitoring a contracted study of the likely fiscal impacts on nine States of elimination of revenue sharing payments to State governments. The Office served as liaison with other organizations such as the General Accounting Office that were considering this issue.

Primary work in preparing Treasury's proposals for the renewal of revenue sharing was carried out in this Office. A number of activities were essential to this effort, including the analysis and evaluation of the effects of modifications in the program's fund-allocation formula, liaison with State and local governments and their interest groups, and preparation of the Secretary's briefing materials and congressional testimony.

#### **Financial Institutions and Capital Markets Policy**

The Office of the Deputy Assistant Secretary for Financial Institutions and Capital Markets Policy includes the Office of Capital Markets Legislation (responsible for the development of administration policy on legislation affecting banks and other financial institutions) and the Office of Securities Markets Policy (primarily concerned with the corporate securities markets and with equity capital formation).

The Office of Capital Markets Legislation was instrumental in developing and securing congressional passage of the President's financial reform

program. The Depository Institutions Deregulation and Monetary Control Act of 1980, which embodied the reforms, became Public Law 96-221 in March. It was the broadest reform of the domestic financial system since the 1930's. The act expanded the Nation's monetary control apparatus by establishing universal reserve requirements for all depository institutions. The concerns of small savers were addressed with the adoption of a program to remove Federal deposit interest rate ceilings within 6 years and authorize nationwide, effective January 1981, negotiable order of withdrawal accounts at all depository institutions. The accounts provide for interest payments on the equivalent of checking deposits. The new act also eased usury ceilings and increased the lending authority and other powers of thrift institutions to enable them to compete more effectively in an increasingly decontrolled market for depository institutions business.

As directed by the Depository Institutions Deregulation and Monetary Control Act of 1980, there was issued in June "The Report of the Interagency Task Force on Thrift Institutions." The report examined in some detail the outlook for thrift institutions in the current financial environment. Capital Markets Legislation was the lead office in staffing and preparing the report.

The Office also prepared and sent to the President an interagency task force study on the relevance of the McFadden Act to present-day banking. The study involved an extensive review of restrictions on intra- and inter-State banking. It identified many of the ways that new technology, banking practices, and fragmentary legislation have eroded the basic thrust of the McFadden Act and other restrictions on banking structure. The study examined alternative proposals to reform the restrictions on geographic expansion of banking activities. The proposals are under review by the President.

In the Securities Markets area, the Office prepared Treasury's position regarding pending legislation which would permit commercial bank underwriting of currently ineligible revenue bonds. The Office participated in passage of the Small Business Investment Incentive Act of 1980 which was designed to facilitate the capital-raising abilities of small businesses. In addition, Treasury's interest in the maintenance of a strong underwriting capability for the securities industry was expressed at the Securities and Exchange Commission hearings concerning the rules of fair practice governing the fixed-price offering of securities.

The Office was involved throughout the year with various other issues, including equity futures contracts under review at the Commodity Futures Trading Commission, the impact on securities markets of the Russian grain embargo, and the Federal Reserve's March credit control actions.

### **Federal Financing Bank**

The Federal Financing Bank (FFB) is a corporate instrumentality of the United States which is subject to the general supervision and direction of the Secretary of the Treasury. It is managed and operated by Treasury employees

who provide services to the FFB on a reimbursable basis. The FFB was established by the Federal Financing Bank Act of 1973 to coordinate, reduce the costs of, and efficiently finance Federal agency and federally guaranteed obligations. The FFB is authorized to purchase any obligation which is issued, sold, or guaranteed, in whole or in part, by a "Federal agency"—defined in the act as any executive department, Federal establishment, corporate or other entity established by Congress and at least partially owned by the U.S. Government.

The act authorizes the FFB to issue its own debt obligations to the Secretary of the Treasury and up to \$15 billion in debt to the public. Current FFB policy is to issue obligations solely to the Treasury and to purchase only direct agency or fully guaranteed obligations. The current FFB lending rate is  $\frac{1}{8}$  of 1 percentage point above its borrowing rate, which is based on the market yield on Treasury obligations of comparable maturity.

Since it began operations in 1974, the FFB has become the vehicle for most eligible Federal and federally assisted borrowings. Current exceptions are the Government National Mortgage Association-guaranteed mortgage pass-through securities, the Department of Commerce-guaranteed title XI ship mortgage bonds, and Chrysler Corp. obligations guaranteed by the Department of the Treasury. These programs are now being financed in the private credit markets. The securities of the farm credit banks, the Federal home loan banks, and the Federal National Mortgage Association are not eligible for purchase by the FFB since these agencies are federally sponsored, not federally owned, and their obligations are not guaranteed by any Federal agency.

As of September 30, 1980, FFB holdings totaled \$82.6 billion, an increase of \$18.3 billion during the fiscal year. Purchases of Farmers Home Administration loan assets accounted for \$6.9 billion (net), or 38 percent, of this increase. Purchases of loan assets from other Federal agencies totaled \$0.7 billion, or 4 percent, of the increase, while FFB purchases of agency direct debt were responsible for 21 percent, or just under \$4 billion net. Net lending under various Federal guarantee programs totaled \$6.8 billion, or 37 percent, of the increase in holdings during the year. The largest guarantee programs involved net loans of \$2.5 billion to rural electric and telephone cooperatives, guaranteed by the Rural Electrification Administration; \$1.9 billion to foreign governments under Department of Defense guarantees; and \$1.1 billion to the Student Loan Marketing Association, guaranteed by the Department of Education.

During fiscal 1980, the FFB began lending to the Central Liquidity Facility (CLF) of the National Credit Union Administration, an off-budget Federal agency. On September 30, 1980, the FFB had just under \$90 million in loans outstanding to the CLF.

In addition, the FFB began lending under three new loan guarantee programs during fiscal 1980. The Tennessee Valley Authority (TVA)



guaranteed loans totaling \$685 million in fiscal 1980, to Seven States Energy Corporation, an entity which leases nuclear fuel to TVA.

The FFB purchased \$119 million of long-term bonds issued by public housing agencies and guaranteed by the Department of Housing and Urban Development pursuant to the United States Housing Act of 1937. The proceeds of the bonds are used by public housing agencies to finance the acquisition, development, or improvement of low-income housing projects. HUD pays part of the interest due FFB on these obligations, representing the difference between the FFB's required interest rate, which is based on taxable Treasury rates and the tax-exempt rate that would be payable if the bond were sold in the market.

The FFB loaned \$1 million in fiscal 1980 under a \$3 million commitment to Jet Industries, Inc., a borrower whose loans are guaranteed by the Department of Energy (DOE) in accordance with the Electric and Hybrid Vehicle Research, Development and Demonstration Act of 1976. The FFB also committed to lend up to \$150 million to borrowers whose loans are guaranteed by DOE under the Geothermal Energy Research, Development and Demonstration Act of 1974. No loans were made in fiscal 1980 under the geothermal program.

FFB net income during fiscal 1980 totaled \$105 million, with administrative expenses of \$640,000 and no operating losses. FFB transferred \$253 million of its accumulated surplus to the Treasury general fund in December 1979, bringing the total of such transfers to \$396 million since FFB's inception.

## ECONOMIC POLICY

The Office of the Assistant Secretary for Economic Policy (OASEP) is responsible for informing the Secretary and other senior policy officials of the Department on current economic developments, advising them concerning prospective economic developments, and assisting them in the development of appropriate domestic economic policies. The office along with the Council of Economic Advisers and the Office of Management and Budget produces official projections of the U.S. economy which serve as the basis for budgetary planning and for choosing among alternative courses of economic policy. The Office of Economic Policy also prepares testimony, briefing, and general background material for the Secretary and Deputy Secretary to use in appearances before congressional committees concerned with economic policies. Staff support for these activities is provided by the Office of Financial Analysis and the Office of Special Studies.

A series of biweekly briefings for the Secretary and other senior policy officials initiated in 1977 continued through 1980. These briefings are coordinated by the Office of Financial Analysis and conducted in cooperation

with other domestic and international offices within Treasury. The briefings consist of analyses of important economic and financial developments of both domestic and international scope and supplement the flow of information provided through other channels.

In addition, OASEP works with the Council of Economic Advisers, the Office of Management and Budget, the Domestic Policy Staff, and various other agencies in analyzing and formulating a number of specific policy initiatives for discussion by the Economic Policy Group. The Office of Special Studies work has included several projects in the energy area, a survey of countercyclical policies, development of anti-inflation program, an analysis of Federal credit programs, and the development of a draft bill on health insurance. OASEP also had a major role in assessing the economic and regional implications of a Chrysler Corp. shutdown.

#### Office of Financial Analysis

The Assistant Secretary for Economic Policy represents the Treasury on the interagency group which develops the official economic forecasts used for the administration's budgetary and economic policy decisions. Other agencies participating in this group are the Council of Economic Advisers, Office of Management and Budget, and the Departments of Commerce and Labor. Staff of the Office of Financial Analysis provided support for the Assistant Secretary in this role and regularly attended meetings of the forecasting group.

Analysis and evaluation of current economic data and information is an essential element in the formulation of economic policy. To support the Department's economic policy function, the Office prepares an Economic Briefing Book which is continuously updated for the Secretary of the Treasury and other high-level Treasury officials. The briefing material provides comprehensive coverage of all of the major economic statistics and includes historical perspectives. Memoranda prepared for the briefing book circulate throughout the Treasury and keep Treasury officials informed of current economic developments.

Supplementing the briefing book, the Office prepares a periodic written summary of economic developments which gives an overview of economic performance and evaluates prospects for the future course of the economy. The Office also has primary responsibility for a biweekly economic and financial briefing for senior Treasury officials. In recent years this has become a major vehicle for the continuing analysis of problems of recurrent interest to Treasury policymakers.

To aid in the formulation of new policy initiatives, the Office from time to time undertakes indepth analysis of special areas of important concern. Studies have recently been undertaken on such topics as the origin and persistence of inflation, investment and its role in stimulating productivity growth, and alternative paths for the domestic economy in the medium term.



As a principal contributor to the formulation of economic policy, Treasury is requested by congressional committees to explain and elaborate upon the economic goals and objectives of the administration. In support of this function the Office has been responsible for overseeing the development of visual and written material for such occasions as the presentation of the Budget to Congress. The Office also prepares briefing and general background material for the Secretary and Assistant Secretary for Economic Policy to use in testifying before the Joint Economic Committee, congressional budget committees, and other committees concerned with economic and financial policies.

Officials of the Department serve as attaches in the embassies and missions to several foreign nations. In order to keep these officials, as well as other Treasury personnel, well informed about current economic developments, the Office circulates relevant material on domestic economic and financial developments.

Public awareness of economic developments and government policies is important to achieving stated goals and objectives. The Office of Financial Analysis conducts briefings and other presentations for a wide range of private groups and organizations on current economic performance and the economic outlook. In addition, the Office has contributed to a broader understanding within Government of the Treasury role in economic policy by making periodic presentations for the Foreign Service Institute.

The Office also provides support for interagency groups or administration programs requiring special expertise. Staff members participated in an interagency task force responsible for assessing current and prospective developments in the U.S. automobile industry. In addition, the Office continued to provide assistance in the Department's monitoring of the Chrysler loan guarantee program, by helping to evaluate compliance of the company's labor agreements with the loan guarantee legislation, and by furnishing analysis of the economic impacts of alternative scenarios of the company's future development.

#### Office of Special Studies

The Office of Special Studies provided a number of analyses and evaluations of economic issues for use by the Secretary, the Deputy Secretary, the Assistant Secretary for Economic Policy, and the Economic Policy Group. It also prepared speeches, testimony, briefing, and other material for use in appearances before congressional committees and public groups. Some of the major areas of concern follow:

*Anti-inflation program.*—Shortly after the President's economic and budget reports were sent to Congress in January, rapid changes in world events and economic prospects made it necessary to intensify the administration's anti-inflation effort. The focus of this effort was primarily on tightening budget policy, credit restraint, and greater conservation of energy. Treasury staff participated in the development of the President's economic proposal of

March 14, 1980, which included a balanced budget, implementation of the Credit Control Act of 1969 to authorize the Federal Reserve to impose new restraints on the growth of credit, and a gasoline conservation fee.

*Countercyclical policies.*—The Tax Reduction and Simplification Act of 1977 utilized an array of countercyclical measures to stimulate the economy including local public works projects, public service employment, antirecession fiscal assistance, and employment tax credits. The Office of Special Studies continues to participate in an interagency effort to evaluate the effectiveness of each of these programs for countercyclical purposes and to refine and adapt the research available for policy planning.

*Budget balance and spending limitation.*—A large number of proposals to set limits on Federal spending, including a constitutional amendment for a balanced budget, were considered by Congress. The Secretary of the Treasury has a major responsibility in formulating the administration's position on these bills and resolutions. The Office of Special Studies participated with the Executive Office of the President in preparing economic and budgetary analyses of these proposals.

*Federal credit programs.*—In the fiscal 1981 budget, the President introduced a system for control of Federal credit programs. The Office of Special Studies continues to participate in an interdepartmental task force providing the various economic and budget analyses required to expand and improve the existing system. Some of the issues being analyzed are the measurement and effect of the subsidies provided by these programs.

*Wage and price standards program.*—The wage and price standards program was modified significantly during 1980 in response to recommendations by the Pay and Price Advisory Committees that were an outgrowth of the national accord reached between the administration and leaders of the labor movement on September 28, 1979. Acceptance of the recommendations by the Council on Wage and Price Stability was often guided by policy decisions of the Economic Policy Group, chaired by the Secretary of the Treasury. At yearend, a review of the program was begun to determine whether or not to continue it, and if so, in what form.

*Industrial policy.*—Substantial weakening in a number of major American industries, most notably steel and automobile, led to a growing proliferation of proposals for industry-specific assistance. Treasury was active in the formulation of these specific proposals, and in a larger effort to develop some overall framework for industrial policies to prevent their being redundant, superfluous, or counterproductive.

*Automobile credit conditions.*—Domestic auto sales fell sharply during the first half of 1980. The Office of Special Studies researched the impact that credit controls may have had on auto sales and prepared background papers for use in policy discussions concerning the auto industry.

*Emergency energy actions.*—Treasury participated with the Department of Energy in further development of the standby motor fuel rationing plan. The

new rationing plan was submitted to Congress under the provisions of the Emergency Energy Conservation Act of 1979, and has been approved.

In conjunction with Department of Energy staff, methods of dealing with a major petroleum supply disruption and their economic impact were studied. The methods studied included price and allocation controls, coupon gasoline rationing, gasoline tax and rebate, and a general rebate of windfall profit taxes.

*Oil import quotas.*—In order to reduce the volume of oil imports, the President directed the Secretaries of Energy and the Treasury to develop jointly a method for limiting oil imports. Treasury staff worked with the Department of Energy to develop a system to hold oil imports to the goal established by the President. Public hearings to consider various alternatives continued into fiscal 1980. Although the administration's program was not adopted, current oil import limitations set by the President are being met.

*Oil security.*—A study of the prospect for oil security was undertaken. The analysis included a projection of oil imports for this decade, a review of the implication of these projections for the vulnerability of the United States in the energy field, and examination of some policy options.

*Synthetic fuels program.*—As part of the national energy program, development of synthetic fuels has been encouraged. Of particular potential is the development of crude oil substitutes from our vast resources of shale and coal. The Office of Special Studies and other Treasury staff participated with the Department of Energy in the preparation of an administration program for the commercial development of synthetic fuels.

*Solar energy.*—Increasing emphasis has been given to energy production from renewable sources such as the Sun. At the direction of the President, Treasury staff participated in a major study effort chaired by the Department of Energy to determine the energy potential available from solar sources and how this potential might be achieved. Treasury's primary contribution in the study included a review of the most appropriate methods for the Federal Government to provide the economic incentives to realize the solar potential.

*Health insurance.*—Congress held a number of hearings and markup sessions on the President's national health insurance draft bill, and the hospital cost containment proposal. The Secretary of the Treasury is a key adviser to the President on national health insurance and hospital cost containment as these issues have implications for the Nation's economic and budget policies. The Office of Special Studies continued to participate in interdepartmental groups on various aspects of these matters and provided economic analysis for various program options as interaction between the administration and Congress proceeded.

*Social security.*—The Social Security Amendments of 1977 call for several rate increases before 1990 which have important economic implications on inflation and the tax burden of employers and employees. The Secretary of the Treasury is managing trustee for the social security trust funds and serves along with the Secretary of Health and Human Services and the Secretary of



Labor on the Board of Trustees. Treasury undertook an analysis of proposals for changes in trust fund financing and benefit structures and their impact on the economy. A paper which examines the indexing of social security benefits was prepared. The impact of current economic forecasts on the financial status of trust funds was also assessed. In addition, Treasury staff participated in the development and review of the economic assumptions and estimates underlying the trustees' annual report on the social security system.

*Study of the labor supply.*—The recent increased emphasis on supply-side issues in macroeconomics relies heavily on the contention that labor supply is highly responsive to changes in the real value of after-tax wages. The Office of Special Studies conducted a review of numerous empirical studies which had used both cross sectional and time series methods to address this issue.

*Government regulation.*—Executive Order 12044, issued March 1978 and extended in June 1980, was a major Presidential initiative to assure that the legitimate goals of Federal regulation are achieved at the least possible cost. As part of the implementation of the Executive order, the Regulatory Analysis Review Group (RARG), a high-level interagency committee that includes Treasury and other economic and regulatory agencies, was created. During fiscal 1980, the RARG reviewed analyses of several major proposed rules including the Environmental Protection Agency's proposed rules on the Clean Air Act visibility standards and the revision of national air quality standards for carbon monoxide; the Department of Energy's building energy performance standards and energy efficiency standards for consumer appliances; and the Department of Education's title VI language minority rules for bilingual education.

## OFFICE OF THE GENERAL COUNSEL

The General Counsel, appointed by the President by and with the advice and consent of the Senate, is the chief law officer of the Department of the Treasury. As the chief law officer, the General Counsel administers the Legal Division, composed of all attorneys performing legal services in the Department and all nonprofessional employees providing support to the attorneys, and is responsible for all of the legal activities of the Department. This includes the legal staffs of all subordinate offices, bureaus, and agencies.

The General Counsel serves as the senior legal and policy adviser to the Secretary of the Treasury and other senior Treasury officials. He reviews the legal considerations relating to policy decisions affecting the management of the public debt, administration of the revenue and customs laws, international economic, monetary, and financial affairs, law enforcement, and other activities. Other responsibilities include providing general legal advice wherever needed, coordinating Treasury litigation, preparing the Depart-

ment's legislative program and comments to Congress on pending legislation, reviewing the Department's regulations for legal sufficiency, and counseling the Department on conflict of interest and ethical matters. The General Counsel also is responsible for hearing appeals to the Secretary of the Treasury from administrative decisions of bureau heads or other officials.

In addition, the Office of Director of Practice (which regulates practice before the Internal Revenue Service) is under the supervision of the General Counsel.

#### Litigation

The Legal Division is responsible for formulating the Department's position on litigation involving Treasury activities and for working with the Department of Justice in the preparation of litigation reports, pleadings, trial and appellate briefs, and assisting in trying all cases in which the Department is involved. The Chief Counsel for the IRS has the litigating responsibility for cases in the Tax Court.

There are many thousand individual cases pending in the Customs Court, the Tax Court, and other Federal courts pertaining to Treasury functions. During fiscal 1980, there was a significant, almost 22-percent, increase over fiscal 1979 in the number of cases filed in the Tax Court.

Significant opinions in the last year are as follows: In *Puerto Rico v. United States* and *Virgin Islands v. United States*, the D.C. Court of Appeals reversed earlier decisions awarding Puerto Rico and the Virgin Islands the proceeds of the 4-cents-a-gallon excise tax imposed on gasoline sold at retail within the United States. The island jurisdictions had claimed that under essentially similar legislation in effect almost since the turn of the century, they were entitled to taxes and customs duties on items manufactured in the island jurisdictions and sold on the mainland. The court held that the statutes in question were basically intended to accord island products treatment equal to that accorded mainland products and not to provide a source of preferential revenue. Potentially, these cases, if decided against the United States, could have required in excess of \$1 billion being withdrawn from the Federal treasury for transfer to the treasuries of the islands to cover past collections and the annual remittance of more than \$200 million to the islands for collections as made.

In the *ITT-Hartford* merger cases, several Hartford stockholders filed motions for summary judgment in the Tax Court and one filed a motion for summary judgment in the U.S. District Court of Delaware, alleging that even if a cash purchase of 8 percent of Hartford's stock by ITT in 1968 and 1969 was part of a plan of reorganization, the subsequent acquisition by ITT of more than 80 percent of Hartford's stock in exchange for ITT's voting stock qualified as a section 368(a)(1)(B) reorganization. Both the Tax Court and the district court granted the motions for summary judgment in 1979. The Government appealed to the first and third circuits. Both circuits reversed the lower courts and held for the Government that a purchase of a portion of



the acquired corporation's stock will invalidate a (b) reorganization, even though more than 80 percent of the acquired corporation's stock was obtained through exchange for the acquiring corporation's voting stock. The cases were remanded to the lower courts for further proceedings. The same issue is pending in the fourth and ninth circuits.

In *Rowan Companies, Inc. v. United States*, the taxability for FICA and FUTA purposes of meals and lodging furnished workers on offshore oil-drilling rigs was in issue. In affirming the district court's summary judgment for the Government, the fifth circuit specifically rejected the reasoning adopted by the seventh circuit in *Oscar Mayer & Co., Inc. v. United States* (7th Cir. 1980) that Congress use of substantially the same definition for "wages" in all their employment tax settings precludes the assertion of FICA and FUTA liability in the admitted absence of income tax withholding liability. Similarly, the fifth circuit took issue with the Court of Claims' decision in *Hotel Conquistador, Inc. v. United States*, 597 F.2d 1348 (Ct. Cl. 1979), *cert. denied* 100 S. Ct. 702, that *Central Illinois Public Service Co. v. United States*, 435 U.S. 21 (1978), prevents FICA and FUTA liability with respect to free meals served to hotel employees. It is expected that taxpayers in *Rowan* will file a petition for certiorari alleging conflict with *Hotel Conquistador*.

In the criminal tax area there were four significant cases. In *United States v. Payner*, the Supreme Court held that the judiciary's supervisory powers do not permit the exclusion of evidence where the traditional tests of standing do not apply. In *United States v. Carlson* (petition for cert. filed), the Ninth Circuit Court of Appeals held that an individual cannot refuse to report income on a tax return on the asserted grounds that such reporting would be incriminating with respect to a prior tax violation. In *United States v. Piester*, the tenth circuit upheld the prosecution of a tax protestor who used the church/vow of poverty defense in a section 7205 prosecution. The court's focus on the issue of the taxpayer's "sincerity" with respect to the church/vow of poverty assertions will be helpful in future such cases. In *United States v. Clardy*, the ninth circuit affirmed the conviction of an individual who in effect developed and sold tax shelter schemes. *Clardy* was essentially a substance over form case where the defendant created a "paper trail" which on the surface would justify certain interest deductions. The case is particularly interesting since the scheme is nearly identical to many cases that in the past have been thought of as strictly civil.

In *EA Shipping Co., Inc. v. Bazemore*, the U.S. Court of Appeals for the Fifth Circuit affirmed a decision of the District Court for the Middle District of Florida which upheld the forfeiture of the M/V EA, a "banana boat" carrying a large quantity of cocaine. The court held the vessel was not a common carrier, but even if it was, forfeiture was not barred because the master had actual knowledge that cocaine was aboard.

During fiscal 1980, numerous cases in the U.S. Courts of Appeals for the First, Fourth, and Fifth Circuits upheld the boarding and search by Customs and Coast Guard officers of foreign-registered "mother ships" on the high

seas, and searches were part of efforts coordinated among various U.S. agencies (State, Justice, DEA, Coast Guard, and Customs) and several foreign governments to stem the flow of drugs to the United States.

In *United States v. Willi Beusch and Dear & Co.*, the U.S. Court of Appeals for the Ninth Circuit in a case of first impression held that a series of currency transactions which, by themselves, constitute only misdemeanors under the Bank Secrecy Act may also constitute felonious activity if they show a pattern of illegal activity and exceed \$100,000 over a 12-month period. The decision also upheld the search and seizure of ledger books and documents pertaining to numerous customers even though only one customer was named in the warrant.

In *International Bonded Warehouses v. Miller*, the U.S. District Court for the D.C. Circuit upheld all aspects of a Customs rule (T.D. 79-1) requiring operators of duty-free stores to produce landing certificates verifying legal entry of commercial quantities of goods into Mexico. The landing certificate requirement is expected to substantially curtail smuggling of "duty-free" goods into Mexico which ultimately end up either in Mexico's black markets or resmuggled into the United States.

In *Mann v. United States*, the U.S. District Court in Texas upheld the right of Customs to refuse to do business with a Customs bonded warehouseman who had refused to respond to Customs communications and had refused to release Government-order merchandise to the district director. The decision has been appealed.

Attorneys have been actively involved in litigation involving the Department's authority over alcoholic beverages under the 21st amendment to the Constitution. In *G. William Miller v. Castlewood*, the Supreme Court vacated and remanded a Court of Appeals decision which held that an ATF ruling concerning alcoholic beverages conflicted with Florida law and that the balance of interests favored upholding the State law over the Federal ruling. On remand, the fifth circuit again ruled in favor of the State statute and reinstated its previous decision. ATF lawyers are currently studying the possibility of seeking Supreme Court review.

In *Goldstein v. Miller*, another case involving the 21st amendment and the issue of Federal v. State, Treasury won a significant victory. The United States District Court for Maryland held that the 21st amendment did not prevent the Federal Government from establishing an exclusive list of liquor bottle sizes which did not include a size permitted by the State of Maryland. This case is currently on appeal with the fourth circuit.

## Regulations

Major regulation projects during the year included the drafting of temporary regulations under the Distilled Spirits Tax Revision Act of 1979 and the alcohol for fuels legislation. Also undertaken were final ingredients labeling regulations, proposed new trade practice and advertising regulations under the Federal Alcohol Administration Act, and implementing regulations

under the new "trafficking in contraband cigarettes" law. The Office participated in drafting Executive Order No. 12170 (November 14, 1979), which blocked Iranian assets after the seizure of the U.S. Embassy in Teheran and the detention of hostages. The order and subsequent order and regulations concerning transactions with Iran were issued under the authority of the International Economic Powers Act. The blocking itself was implemented by Treasury's Office of Foreign Assets Control. The Office of the General Counsel played a very active supporting role.

#### Finance

The Office of the General Counsel participated in legal and policy discussions with respect to Chrysler Corp.'s request for Federal assistance and New York City's request for additional guarantees. The Office participated in the development of the legislation which created the Chrysler Corp. Loan Guarantee Board, which is chaired by the Secretary of the Treasury. The General Counsel of the Department served as the General Counsel of the Chrysler Corp. Loan Guarantee Board. The Chrysler program entailed the negotiation of the restructuring of approximately \$4 billion in debt and has been called one of the most complicated financial transactions in history. The negotiations were conducted with domestic banks and other financial institutions, European banks, Japanese banks, Canadian banks, the States of Michigan, Indiana, and Delaware, and the Governments of Canada and the Province of Ontario. The Office served as staff to the Board and assisted in the preparation of the documentation required to support the findings required by the statute before the Chrysler Corp. qualified for federally guaranteed assistance.

The Office participated in the issuance of additional guarantees to New York City pursuant to the New York City loan guarantee program. The Office participated in legal and policy discussions regarding the timing of the guarantees and the analysis of the city's budget and financial outlook. This activity represented a further implementation of the New York City Loan Guarantee Act of 1978.

The Office participated in a task force which led to the passage of the Energy Security Act and the creation of the U.S. Synthetic Fuels Corporation. Activities included the participation in intra-agency discussions regarding the need for, and the structure of, the organization, and with staff of the Senate Energy Committee. Activities also included participation on a task force on the implementation of the provisions of the act and the interim program in the Department of Energy mandated by Congress.

The Office participated in a joint study conducted by the Treasury, the Federal Reserve Board, and the Securities and Exchange Commission regarding the need for, and possible structure of, regulation with respect to the GNMA forward market. Activities included participation in interviews conducted with members of the dealer and investment community and legal and policy advice concerning alternative structures for a regulatory oversight



mechanism. A draft report summarizing the findings of the study group and their proposed recommendations has been developed and circulated for comment.

The Office served as counsel to the Federal Financing Bank in connection with its lending activities.

#### Legislation

During fiscal 1980, the General Counsel received 1,031 requests and provided the Department's views to Congress and the Office of Management and Budget on about 700 to 800 bills, draft proposals, and legislation-related items concerning nontax matters. In addition, the Office participated in drafting a number of legislative proposals which became law during this period. Among the more significant were:

1. Chrysler Corporation Loan Guarantee Act of 1979 (Public Law 96-185).
2. Increased participation by the United States in the Inter-American Development Bank, the Asian Development Bank, and the African Development Fund (Public Law 96-259).
3. Increased participation by the United States in the International Monetary Fund (Public Law 96-389).
4. Energy Security Act, providing funds for the development of synthetic fuels (Public Law 96-294).
5. Temporary debt ceiling increases (Public Laws 96-264 and 96-286).

#### Personnel

The enactment of the Civil Service Reform Act of 1978 has greatly increased the need for attorney involvement in Federal personnel administration, particularly in the areas of labor-management relations, employee relations, and equal employment opportunity matters. The act, to a significant degree, relies upon third-party procedures to resolve labor-management disputes, employee relations appeals, and EEO complaints and also contemplates judicial review of decisions in these areas to a greater extent than ever before. To assure appropriate legal review and representation, the General Counsel and the Assistant Secretary (Administration) entered into a comprehensive agreement effective June 26, 1980, under which counsel reviews all final agency EEO decisions prior to approval, reviews proposed adverse actions, and provides representation in the cases involving the Office of the Secretary before the Merit Systems Protection Board and the Federal Labor Relations Authority.



## ENFORCEMENT AND OPERATIONS

The Assistant Secretary (Enforcement and Operations) was assisted by two deputies and their staffs in the oversight and supervision of four operating bureaus: U.S. Customs Service, U.S. Secret Service, Federal Law Enforcement Training Center, and Bureau of Alcohol, Tobacco and Firearms. The policies and operations of the Office of Foreign Assets Control were also under the purview of the Assistant Secretary.

The Office of Operations continued to be primarily concerned with the zero-base-budget objectives program emphasizing regular top management review sessions with the bureaus, cost-effective execution of programs, productivity improvements, equal employment opportunities, legislative review, and various policy issues regarding the bureaus. In addition, the Office of Operations provided leadership in the policy decisionmaking process regarding the zero-base budgets of each of the four operating bureaus under the supervision of the Assistant Secretary.

As a result of an analysis of the alcohol strip stamp program by the Office of the Secretary staff, the Bureau of Alcohol, Tobacco and Firearms was able to realize a savings of approximately \$1,300,000 in 1980 with further estimated savings of \$454,000 and \$104,000 in 1981 and 1982, respectively.

The staff of the Deputy Assistant Secretary (Enforcement) continued its review of policies and standards under which Treasury law enforcement personnel perform their duties. Guidelines on the development and use of informants and undercover operations were forwarded to the bureaus and comments are currently being analyzed. The Office of Foreign Assets Control has been involved in implementing Executive Order 12065 blocking Iranian assets since November 14, 1979.<sup>1</sup> A census of all outstanding claims by U.S. nationals against Iran was conducted by the Office. Also, a census was conducted of those assets blocked under the Executive order.

The activities of each of the bureaus and the Office of Foreign Assets Control are recorded in the "Administrative Reports" section of this volume.

### Alcohol ingredient labeling

Treasury issued in June 1980 final rules requiring importers and producers of alcoholic beverages either to include on the label a partial list of ingredients used in the product, or to provide a label statement informing consumers where they can obtain the ingredient list. The rules become effective January 1, 1983.

### Health warning labels

A final report to Congress and the President on "Health Hazards Associated with Alcohol and Methods to Inform the General Public of these Hazards" has been prepared in compliance with the Comprehensive Alcohol

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<sup>1</sup> See exhibit 40.

Abuse and Alcoholism Prevention, Treatment, and Rehabilitation Act Amendments of 1979 (Public Law 96-180). Section 19 of the act states that the Departments of Treasury and Health and Human Services (HHS) shall jointly submit a report on: (1) The extent and nature of birth defects associated with alcohol consumption by pregnant women; (2) the extent and nature of other health hazards associated with alcoholic beverages; and (3) the actions which should be taken by the Federal Government under the Federal Alcohol Administration Act and the Federal Food, Drug, and Cosmetic Act with respect to informing the general public of such health hazards. In order to meet the requirements of Public Law 96-180, the Departments pursued two courses: A thorough review of the scientific literature and consultation with individuals knowledgeable about the health hazards associated with alcohol and ways to inform the general public of these health hazards. To achieve this goal, a number of steps were taken. A Federal Register notice was announced on February 26, 1980, and 158 comments were received and analyzed by staff of both Departments. Nine formal consultations with leading medical experts, representatives of the alcoholic beverage industry, communications specialists, experts from the fields of alcoholism and traffic safety, and other interested parties, such as consumer groups were held with high-level officials and staffs from both Departments. Also, numerous informal consultations with other experts and representatives of Government agencies with expertise were made by staffs from the Departments of Treasury and Health and Human Services.

An interim report was submitted by the Departments on June 1, 1980. It contained a request for an extension in order to analyze and utilize materials collected from the consultations and comments submitted in response to the Federal Register notice.

Part I: "Birth Defects and Anomalies"—summarizes current knowledge about the fetal alcohol syndrome, birth defects, and other alcohol-related risks to unborn children and postnatal development.

Part II: "Other Health Hazards"—summarizes a range of physical, mental, and emotional illnesses and disabilities associated with the misuse of alcohol including alcoholism, and other alcohol-related hazards, such as accidents.

Part III: "Informing the Public about Health Hazards"—contains the following recommendations:

1. Government, industry, and private organizations should develop and conduct a broad-based, diverse, and highly visible public information campaign on alcohol-related health problems. To the extent possible, the combined campaign should be built upon a common strategy.
2. In consultation with Government, industry should develop an effective slogan and/or logo, or a family of related slogans or logos, to lend verbal or visual identity to the elements of the

- campaign. Alcoholic beverage producers should voluntarily use the slogan and/or logo in consumer product information.
3. HHS will expand its current efforts to inform and educate the public regarding major alcohol-related health hazards; Treasury will continue its current efforts to inform and educate the public regarding effects of alcohol consumption during pregnancy and continue to work with industry to monitor and encourage the Beverage Alcohol Information Council's Fetal Alcohol Awareness Campaign.
  4. HHS will work with the Department of Education, voluntary groups, State agencies, and industry groups concerned with alcohol education to increase the use of model alcohol curricula on the local level.
  5. HHS will develop a public information program aimed at women who are pregnant or plan to become pregnant with advice on how to protect the health of their children. This will include appropriate advice about the rules of alcohol use.
  6. HHS will encourage the accurate portrayal of alcohol-related health hazards in the print and broadcast media.
  7. Treasury, while recognizing the important efforts that some segments of the alcoholic beverage industry have taken to control their advertising practices, will encourage other industry members to review the impact of their advertising practices on alcohol-related health hazards and revise their voluntary codes of advertising as appropriate. The question of whether the Congress should place additional restrictions on alcoholic beverage advertising should continue to be considered.
  8. HHS and Treasury will support the National Highway Traffic Safety Administration in its efforts to promote programs to discourage driving while under the influence of alcohol.

The Departments are convinced that public awareness and understanding would be enhanced if the alcoholic content were consistently and clearly indicated on all domestic and imported alcoholic beverages. The consumer could then, at least, comparatively evaluate the products. The Departments recommended that a uniform alcohol content statement be required for all alcoholic beverages, and that alternative measures of content be explored to determine the most useful.

1. Congress should amend the FAA Act to require malt beverages to be labeled to disclose the alcohol content as a percent by volume.
2. Require distilled spirits to be labeled for alcohol content as a percent by volume.
3. Congress should amend the FAA Act to require all wines to be labeled to disclose the alcohol content as a percent by volume.

Health professionals should be a primary source of information about health hazards associated with alcohol. Yet, during the departmental



consultations, physicians confirmed that most lack training regarding health consequences of alcohol use and many are unaware of the recent research findings about the five major health hazards discussed in the report. The lack of current information was particularly troublesome respecting fetal alcohol effects. The Departments recommended the following action:

1. The Surgeon General will issue an advisory on the major health problems discussed in the report.
2. HHS will encourage States to require that health care and other appropriate professionals seeking State licenses and recertification demonstrate their knowledge of alcohol-related health hazards.
3. HHS will increase its support for development of curricula about the health consequences of alcohol consumption, and will encourage incorporation of such curricula into the basic professional education for physicians, nurses, pharmacists, social workers, and other health care delivery system professionals.
4. HHS will encourage the development of more sophisticated social and medical screening techniques to improve identification of individuals at high risk for alcohol-related health hazards.
5. The Food and Drug Administration (FDA) will intensify its efforts in reviewing and updating prescription and over-the-counter drug labeling to inform the health care professional and patient about the potential of alcohol-drug interactions.
6. FDA will continue other informational activities.

#### **Alcohol fuel production**

The Energy Tax Act of 1978 instructed the Secretary of the Treasury to furnish to Congress recommendations for simplifying and expediting procedures for those desiring to make alcohol for use as a fuel. Treasury, working with Members of Congress, developed legislation which Congress enacted as part of the Crude Oil Windfall Profit Tax Act of 1980 (Public Law 96-223). The act permitted the Secretary of the Treasury to waive provisions of the Internal Revenue Code for alcohol fuel plants, except for the payment of taxes.

On June 20, 1980, Treasury published temporary regulations providing for the establishment of distilled spirits plants solely for the purpose of producing, processing, and storing, and using distilled spirits for fuel. The regulations substantially reduced the requirements covering security, bonding, recordkeeping, and other matters, but they varied depending on the plant's production level (small, medium, and large). In addition, application procedures were also simplified. These changes gave special attention to assisting relatively small producers such as farmers and farm cooperatives.

Treasury will issue final regulations after consideration of the comments received during the comment period. Most comments received, however, appear not to require significant changes to the temporary regulations. ATF plans to publish the final regulations in February 1981.



### U.S.-European Community wine consultations

Access of American wines to European markets has been limited by strictly interpreted European Community (EC) rules governing wine labeling and production. Since 1974, the United States and the EC have held annual technical consultations to deal with the problems. In the past the results of these consultations were limited. However, over the last year substantial progress was made. Through administrative action and amendments to the EC regulations, the United States has successfully obtained EC's acceptance or recognition of many U.S. standards and practices. The resolution of these problems will increase U.S. producers' access to European markets.

An interagency committee,<sup>2</sup> chaired by Treasury, aggressively approached the spring 1980 consultations and was successful in obtaining from the Community agreement to:

- Allow the use of strip labels on U.S. wines to provide EC mandatory information commonly lacking on U.S. wine labels (e.g., Product of the U.S.A.);
- Add 18 additional U.S. grape varietal names to the list of permitted imports (among them is the major commercial variety "French Colombard"); and
- Amend EC regulations 1608/76 providing de facto recognition of U.S. standards (minimum acceptable percentages) for varietal wines, appellation wines, and vintage dating.

In addition, through a series of technical discussions, the number of outstanding differences in U.S. and EC enological practices has been narrowed. As a result of this ongoing work, the problem will hopefully be resolved, within a year, eliminating another major barrier to U.S. products.

The discussions have helped to obtain a more flexible EC attitude towards the importation of U.S. wines. Channels of communication have been developed that can now be used by both sides to expedite the resolution of specific problems and should lead to the harmonization of U.S. and EC regulations in the future.

### Bank Secrecy Act of 1970

Under Treasury regulations (31 CFR part 103) issued to implement the (Foreign) Bank Secrecy Act (titles I and II of Public Law 91-508), financial institutions, including banks and brokerage firms, are required to maintain certain basic records that may be required to document basic financial transactions. The regulations also require reports concerning foreign financial accounts, large domestic currency transactions, and the international transportation of monetary instruments.

The Assistant Secretary (Enforcement and Operations) has been delegated responsibility for the general supervision of the enforcement and administra-

<sup>2</sup> Departments of Agriculture, State, and Commerce, and United States Trade Representative.

tion of the regulations. Responsibility for specific areas of compliance has been delegated to the Federal bank supervisory agencies, the Federal Home Loan Bank Board, the National Credit Union Administration, the Internal Revenue Service, and the U.S. Customs Service.

During fiscal 1980, there was a great deal of congressional interest in the implementation of the act and the administration of the related regulations. The Assistant Secretary and his representatives testified before various House and Senate committees.<sup>3</sup>

A major area of interest to the congressional committees was the unusual flow of currency in Florida initially reported by the Assistant Secretary in 1979. During calendar 1978, the Federal Reserve bank offices in that State had an excess of receipts and removed \$3.2 billion in currency from circulation. For calendar 1979 that figure rose to \$4.9 billion. Much of the currency appears to be related to the drug traffic and other illegal activity.

Treasury has taken a number of actions to counteract this unusual activity, including the amending of the regulations governing the reporting of currency transactions by banks and other financial institutions.<sup>4</sup> In addition, the Department has, in cooperation with the Department of Justice, established a currency flow project in Florida to investigate the activities related to the huge surplus of currency. The principal participants are the IRS, Customs, the Federal bank supervisory agencies, and the Department of Justice. Both civil and criminal investigations are underway currently and will continue into fiscal 1981.

Significant improvements were made in the computerization of forms 4789 during the year. The IRS has centralized that responsibility at the IRS Service Center in Ogden, Utah, and new processing procedures are being developed. For the first time, since the reporting requirement became effective in 1974, incomplete forms will be returned to the financial institution for perfection.

During fiscal 1980, 232,000 IRS Forms 4789 (Currency Transaction Reports) and 94,000 Customs Forms 4790 (Report of International Transportation of Currency or Monetary Instruments) were filed with the Department. The Department provided the Drug Enforcement Administration with 714 reports reflecting \$188.7 million in transactions and 499 reports pertaining to the international transportation of currency and other monetary instruments totaling \$612.4 million that appeared to be drug related. A substantial number of reports were also furnished to other Federal agencies and to congressional committees. There were 54 convictions resulting from Customs investigation of criminal violations of the act, and Customs made 1,102 seizures of unreported monetary instruments totaling more than \$28.3 million.

<sup>3</sup> See exhibit 43.

<sup>4</sup> See exhibit 44.

### Counterterrorism

Treasury has continued its active participation in the Executive Committee on Terrorism of the National Security Council's Special Coordination Committee and in interagency Federal security planning for special events. The Department and its enforcement agencies were heavily involved in the security planning for the 1979 Pan American Games in Puerto Rico and the 1980 Winter Olympics in Lake Placid, N.Y. Treasury and the Department of State have also been giving increased emphasis to the problems of protecting foreign diplomatic facilities in the United States.

### Reimbursement for diplomatic protection

Public Law 94-196 authorizes the Secretary of the Treasury to reimburse State and local governments for certain costs of protecting foreign diplomatic missions under special conditions. Implementing regulations were first adopted in 1976. However, the Department's experience in administering the regulations indicated a need to modify them in order to clarify certain areas of ambiguity and to define more clearly the scope of the reimbursement. Without such changes, the full amount of reimbursements permitted by the statute could not be made.

In May 1980, the revised regulations implementing Public Law 94-196 were published. The principal improvements that they accomplished are:

- Extended protective perimeters outside of the immediate area of a foreign mission can now be reimbursed.
- Fixed security posts assigned at foreign missions because of an extraordinary protective need can now be reimbursed.
- Administrative and overhead costs for extraordinary security can be reimbursed at a fixed rate of 18 percent of the total extraordinary protection cost or on a dollar-for-dollar basis.
- Retroactive application of the revised regulations will be made when a local government resubmits claims that may have been insufficiently reimbursed under the former regulations.
- Under Public Law 96-74, security for motorcades and at other places associated with the visit of a foreign dignitary may be reimbursed.

## TAX POLICY

### Legislation

*The Crude Oil Windfall Profit Tax Act of 1980.*—The Crude Oil Windfall Profit Tax Act of 1980 (Public Law 96-223), proposed April 26, 1979, was enacted April 2, 1980. The tax applies generally to three categories or tiers of oil: Oil previously subject to price controls; stripper oil; and newly



discovered, incremental tertiary, and heavy oil. These categories are taxed at rates of 70, 60, and 30 percent, respectively, on receipts which exceed bases established for each tier or at lower rates on some oil production of independent producers. The tax is to phase out when net receipts reach \$227.3 billion, but beginning no later than January 1, 1991, or earlier than January 1, 1988.

The President is required to recommend to the Congress the manner in which net windfall profit tax receipts are to be allocated among programs to provide energy assistance to the poor, finance transportation and conservation programs, and provide income tax reductions.

As part of the act, increased personal and business tax subsidies are provided for conservation investments and the production of fuels from renewable and exotic sources. In addition the act contained three income tax provisions: A \$200 exclusion for interest and dividends (\$400 for married couples), repeal of carryover basis, and changes to last-in, first-out (LIFO) accounting rules.

*Comprehensive Environmental Response, Compensation and Liability Act of 1980.*—Public Law 96-510, approved after the close of the fiscal year on December 11, 1980, established a program for the cleanup of releases of hazardous substances into the environment and for payment of damages to Government-owned natural resources. The law reflects a recommendation of the President of June 1979.

Title II of the law imposes taxes on crude oil and 42 specified chemicals for the period April 1, 1981–September 30, 1985. The taxes terminate when aggregate collections reach \$1.38 billion if earlier than September 30, 1985. A hazardous substance response trust fund also is created to receive the receipts from the taxes, recoveries from responsible parties of amounts expended for cleanup and damage costs paid for by the Government, and certain minor items. In addition, there is authorized to be appropriated \$44 million a year to the fund from general revenues. Monies in the trust fund are to be used for cleanup costs and payment for damages to Government-owned natural resources.

Another provision establishes a tax on hazardous waste and a post-closure liability trust fund. The tax is levied on each ton of hazardous waste received at a qualified hazardous waste disposal facility between October 1, 1983, and September 30, 1985, but no tax is to be levied in any calendar year following any year on September 30 of which the unobligated balance of the fund exceeds \$200 million. The trust fund is to receive such amounts as may be appropriated thereto. The fund is to assume the liability originally imposed on the owner of the waste site after its closure if certain requirements are met.

Multiemployer Pension Plan Amendments Act of 1980 (Public Law 96-364), approved September 26, 1980, amends the Internal Revenue Code and Employee Retirement Income Security Act (ERISA) to improve retirement income security under private multiemployer pension plans.



Technical Corrections Act of 1979 (Public Law 96-222), approved April 1, 1980, contains technical amendments to Public Laws 95-600, 95-615, 95-488, and 95-618.

Public Law 96-298, approved July 1, 1980, provides for a 3-month extension of excise taxes for the airport and airway trust fund. Public Law 96-283, approved June 28, 1980, imposes an excise tax on the removal of a hard mineral resource from the deep seabed.

Public Law 96-84, approved October 10, 1979, extends to January 1, 1982, the temporary exclusion from Federal unemployment taxes for agricultural services provided by certain alien individuals. Public Law 96-167, approved December 29, 1979, continues prohibitions against issuing rules relating to fringe benefits, commuting expenses, and State legislators' travel expenses. It also makes some noncontroversial and simplification amendments to the tax code; e.g., eliminates filing requirements for certain stock options, provides for payment of interest on wrongful levies, extends the time for filing fourth-quarter gift tax returns. Public Law 96-178, approved January 2, 1980, extends for 1 year provisions relating to business expenses of State legislators (these provisions were, however, nullified by Public Law 96-167). The act also modifies the work incentive credit provisions. Public Law 96-272, approved June 17, 1980, revises and makes permanent special rules relating to child day care services and the WIN tax credit.

#### General tax policy

Reduction of inflation was the first priority of economic policy for 1980. The budget for fiscal 1981, presented in January 1980, proposed fiscal discipline, combined with policies designed to alleviate the underlying structural causes of inflation in the areas of energy productivity, investment, and Government regulation. The principal tax provisions in the budget included the energy program, consisting of energy tax credits and the windfall profit tax on oil, cash management initiatives, affecting both individuals and corporations, and restrictions on tax-exempt housing bonds. These measures provided for increased receipts of \$6.4 billion in fiscal 1980 and \$21 billion in fiscal 1981.

In March, as part of his anti-inflation program, the President announced two new revenue-increasing measures: A gasoline conservation fee of \$4.62/barrel on imported crude oil and the introduction of tax withholding on interest and dividends. These measures would have increased receipts in fiscal 1981 by approximately \$13 billion.

In August, the President announced the details of his economic revitalization program. This program was designed to create half a million jobs by the end of 1981 and a total of 1 million jobs by the end of the following year. Cost-reducing and productivity-enhancing provisions were designed to boost investment by 10 percent, speed the recovery, and result in real economic growth of 4 to 5 percent per year without rekindling inflation. Its tax provisions included: Liberalization and simplification of depreciation, making

the investment tax credit partially refundable, providing an individual tax credit to offset social security tax rises, liberalization of the earned income credit, a targeted investment tax credit to assist depressed areas, rapid amortization of startup costs for small business, and some relief from the marriage penalty. These provisions all together would have reduced tax liability by \$27.6 billion in calendar 1981, rising to \$58.3 billion in 1985.

*Dividend and interest withholding.*—In March 1980, as part of the "Fiscal Year 1981 Budget Revisions," President Carter proposed that payments of interest and dividends be subject to withholding at a rate of 15 percent.<sup>1</sup> Exempted from such withholding would be payments to individuals who reasonably believed that they would owe no tax, to corporations, and to tax-exempt individuals.

No new tax would be imposed upon dividend and interest income. The proposal was designed primarily to insure that those individuals who fully report their income are not required to bear an increased tax burden because other individuals should, but do not, report all their income. In 1979 it was estimated that taxpayers underreported interest and dividend income by about \$16 billion and thereby underpaid their taxes by approximately \$3.6 billion. At the end of fiscal 1980, this legislation had not been reported out of the House Ways and Means Committee.

*Cash management initiatives.*—The fiscal 1981 budget contained several proposals to alter the timing of tax payment dates, balancing the benefits of more rapid tax collection against administrative costs. Generally, smaller payments would be made less frequently, and larger payments would be made more frequently and closer to the time at which the liability is incurred. Overall, these initiatives would increase receipts and decrease Government borrowing costs by \$5.1 billion in fiscal 1981, \$6.7 billion in 1982, and \$3.5 billion in 1983.

In February, the House Ways and Means Committee held a hearing on those proposals. Two of the four proposals that could be implemented administratively are scheduled to become effective by January 1981. Deposits of FICA (social security) taxes by State and local governments are accelerated to put them on a basis closer to that of private employers. Congress acted to modify slightly the regulations implementing this change. The new schedule, as modified by Congress, became effective in July 1980. The timing of employer deposits of withheld income and FICA taxes was altered giving relief to about 1 million employers while accelerating deposits for fewer than 60,000 of the largest employers. Proposed regulations were published for comment, a public hearing was held, and final regulations were issued. Regulations requiring large tobacco manufacturers to pay their tobacco excise taxes faster and more frequently and a separate proposal that requires large payments of alcohol and tobacco excise taxes to be paid by electronic funds transfer rather than by mail were under consideration.

<sup>1</sup> See exhibit 50.

Various changes are under study to accelerate payments of customs duties. No definite action was taken during the year.

Two proposals required legislation. The portion of individual income tax liability which must be paid currently would be increased from 80 percent to 85 percent. The group of taxpayers excused from paying estimated taxes would be expanded from those with less than \$100 in unpaid tax liability to those with less than \$300 in unpaid liability. Congress did not take any action on this proposal.

Several changes were proposed for corporate income tax payments. The required level of estimated income tax payments would be increased from 80 percent to 85 percent of final liability. Large corporations which currently are excused from meeting the 80-percent rule if doing so would require estimated tax payments to exceed the prior year's liability would be required to pay estimated taxes of at least 60 percent of the current year's liability. The quarterly estimated tax payment dates would be altered to permit the Federal Government to make better use of available cash without imposing additional costs on corporations. The final payment of any remaining tax liability would be due 2½ months after the close of the tax year. As part of the 1981 budget reconciliation bill, the House-Senate Conference decided to require large corporations to pay at least 60 percent of their liability currently regardless of the prior year exceptions.

*Alcohol fuels.*—The Energy Tax Act of 1978 exempted from excise tax, for the period January 1, 1979, through September 30, 1984, motor fuels containing at least 10 percent of 190-proof alcohol (other than alcohol made from petroleum, natural gas, or coal), a mixture commonly called gasohol.

If the motor fuel mixture contained exactly 10 percent alcohol, the exemption from the 4-cents-a-gallon excise tax was equivalent to subsidy of 40 cents a gallon for the alcohol. However, there was no exemption for motor fuel containing alcohol if the proportion was less than 10 percent; and if it contained more than 10 percent, the subsidy equivalent for the alcohol content was less than 40 cents a gallon. Furthermore, where the fuel without regard to its alcoholic content was directly, or indirectly, exempt from tax because of the status of the buyer or the nature of the use (e.g., a sale to a State or local government or for use on a farm), the alcohol fuel exemption was of no consequence.

The Crude Oil Windfall Profit Tax Act of 1980 equalized the treatment of alcohol in fuels of different alcoholic content or in cases where the fuel was otherwise exempt from tax by providing for a nonrefundable income tax credit of 40 cents a gallon for alcohol of 190-proof or greater (other than that made from petroleum, natural gas, or coal) for the period October 1, 1980, through December 31, 1992, when used by a taxpayer as a fuel or in a trade or business, sold at retail by the taxpayer by placing it in the fuel tank of the purchaser's vehicle, or when mixed with gasoline or any other motor fuel and sold or used by the taxpayer in a trade or business. The credit is 30 cents a gallon if the proof is less than 190 but not less than 150-proof. While the credit



is nonrefundable, a 7-year carryover for unused credit is granted. The credit is reduced to take account of any benefit from the gasohol exemption which was extended through 1992.

*Airport and airway trust fund taxes.*—The airport and airway trust fund was scheduled to expire on June 30, 1980, and taxes financing the fund were scheduled to expire or be reduced at the same time. The President's fiscal 1981 budget repeated his 1980 recommendation to extend the fund and taxes from 1980 to 1990. The taxes on air passenger and freight transportation would have been extended at the existing rates. The 7-cents-per-gallon tax on aviation fuel would have been changed to an ad valorem tax of 10 percent of the retail price. New taxes of 6 percent on retail sales of planes and avionics for domestic noncommercial aviation use also were included.

Since Congress had not finished action on revising and extending the trust fund and the air user taxes by June 30, Public Law 96-298, approved July 1, extended them through September 30. While the tax committees of Congress also had recommended somewhat different bills extending the taxes and trust fund beyond September 30, no further congressional action was taken and the trust fund and air user tax system expired as of October 1. The taxes on transportation of property, international departures, jet fuel used in noncommercial aviation, and the annual aircraft registration fee expired. The tax on transportation of persons was reduced from 8 percent to 5 percent, and the tax on gasoline used in noncommercial aviation was reduced from 7 cents a gallon to 4 cents.

#### Administration, interpretation, and clarification of tax laws

During fiscal 1980, 58 final Treasury decisions, 18 temporary Treasury decisions, and 68 Treasury notices of proposed rulemaking were published in the Federal Register. A substantial number of these publications implemented provisions of the Crude Oil Windfall Profit Tax Act of 1980, the Revenue Act of 1978, and the Tax Reform Act of 1976. Typical items included regulations relating to the "gas guzzler" tax, vesting and nondiscrimination requirements for qualified plans, and generation-skipping transfers.

#### Publications

*Tax reports.*—Pursuant to various congressional and other requirements, the Treasury published the following reports in fiscal 1980:

"Territorial Income Tax Systems," October 1979.

"Equitable Tax Treatment of United States Citizens Living Abroad," January 1980.

"The Operation and Effect of the Domestic International Sales Corporation Legislation," the 1978 annual report, April 1980.

"The Operation and Effect of the Possessions Corporation System of Taxation," the third annual report, June 1980.

"First Progress Report of Study on Highway Excise Tax Structure," September 1980.



George N. Carlson, "Value Added Tax, the European Experience and Lessons for the United States," October 1980.

*Tax research.*—The Office of Tax Analysis published the following papers in 1980 on the economic effects of tax systems:

Eugene Steuerle, "Equity and the Taxation of Wealth Transfers," June 1980 (OTA Paper No. 39)

George N. Carlson, "International Aspects of Corporate-Shareholder Tax Integration," July 1980 (OTA Paper No. 40)

#### Tax treaties<sup>2</sup>

New or revised income tax treaties were signed with Malta (March 21, 1980), Cyprus (March 26, 1980), Jamaica (May 21, 1980), Denmark (June 17, 1980), Egypt (August 24, 1980), and Canada (September 26, 1980). The income tax treaty with Bangladesh will be signed in early fiscal 1981. The revised income tax treaty and protocols with the United Kingdom entered into force on April 25, 1980.

In addition, negotiations or correspondence with respect to proposed income tax treaties or protocols continued with Argentina, Brazil, Germany, Indonesia, Italy, Tunisia, the Soviet Union, and the United Kingdom. And negotiations to revise existing income tax treaties were initiated with Austria, Belgium, the British Virgin Islands, the Netherlands Antilles, Switzerland, and Trinidad and Tobago.

Estate tax treaty negotiations with Austria, Denmark, and Germany resulted in agreement in each case on a proposed text to be submitted to the Department of State requesting approval and signature. New estate tax treaties entered into force with the United Kingdom on November 11, 1979, and with France on October 1, 1980. The estate tax treaty with Canada is repealed by the terms of the income tax treaty with Canada signed on September 26, 1980; however, the latter treaty covers estate taxes to some extent for purposes of the exchange of information. It was agreed that estate tax treaty negotiations with Italy will be scheduled in fiscal 1981.

#### Participation in international organizations

Treasury representatives participated in the work of the Committee on Fiscal Affairs of the Organization for Economic Cooperation and Development (OECD), including membership on a number of working parties of the Committee. Treasury representatives also participated in the U.N. Group of Experts on Tax Treaties between Developed and Developing Countries.

Treasury representatives also meet annually with tax authorities from the United Kingdom, the Federal Republic of Germany, and France to study more effective methods of avoiding double taxation, simplification of arrangements for the assistance of taxpayers through mutual consultation, and the exchange of tax-related information.

<sup>2</sup> See exhibit 49.

## INTERNATIONAL AFFAIRS

### Trade and Investment Policy

#### Trade issues

In fiscal 1980, Treasury was particularly active, in coordination with the U.S. Trade Representative's office, in the implementation of the results of the Tokyo Round of multilateral trade negotiations (MTN), concluded in Geneva in April 1979. The U.S. Government was active in encouraging other countries, especially developing countries, which have not already done so, to sign the codes on nontariff barriers to trade. Implementation of these codes should lead to a more stable and open world trade environment. By the end of the fiscal year, 21 developed, 10 developing, and 2 Socialist countries had signed one or more of the codes.

The Treasury took a special interest in the accession of developing countries to the Agreement on Subsidies/Countervailing Measures, one of the key codes on nontariff barriers agreed upon during the MTN. Six developing countries have signed the code, and others are contemplating signing. Bilateral consultations were held with a number of developing countries regarding the assumption of code commitments on export subsidies by these countries. As a result, less developed countries (LDC's), as well as developed countries, have contributed to a strengthened international discipline on subsidies.

Most of the new codes on nontariff barriers to trade entered into force January 1, 1980. These include the codes on subsidies and countervailing measures, import licensing, technical barriers to trade (Standards Code), and antidumping. Governments participating in the MTN also negotiated agreements on trade practices with respect to particular products—civil aircraft, bovine meat, and dairy products—which became effective on January 1, 1980, as well. The code on customs valuation entered into force between the United States and the European Community on July 1, 1980; for other signatories it will enter into force January 1, 1981. The Government Procurement Code is also scheduled to go into effect on January 1, 1981.

The U.S. Government held extensive discussions with the Japanese regarding their implementation of the Government Procurement Code in fiscal 1980. The United States has encouraged Japan to expand the amount of government purchases to be included in the code, in particular purchases by Nippon Telephone and Telegraph. The U.S. Government, along with other code signatories, also held consultations with several other countries, with a view towards increasing the value of their offers of government purchases to be included under the code.

As part of their implementation of the MTN, the United States and other signatories also began the staged reduction of tariffs. The developed countries have agreed to reduce their tariffs an average of 33 percent over an 8-year period (tariffs on most items will be reduced immediately for the least developed of the developing countries).

The Organization for Economic Cooperation and Development (OECD) countries renewed their commitment to reducing trade barriers by signing a permanent Declaration on Trade Policy, replacing the OECD trade pledge. The June 4, 1980, declaration commits OECD members to avoid restrictive trade and current account measures, effectively implement the MTN, continue work in areas not covered by the MTN, strengthen trade relations with the LDC's, and facilitate positive adjustment to structural changes in world demand and production.

Treasury was involved in other important import issues during the fiscal year.<sup>1</sup> It participated in an interagency task force which considered various trade options for the U.S. Government in the case of steel imports. In March 1980 the Government suspended the trigger price mechanism (TPM), set up by Treasury in 1978. The suspension followed the filing by U.S. Steel of a formal dumping complaint with the U.S. International Trade Commission (USITC) against imports from seven European nations. The U.S. Government reinstated the TPM on October 21, 1980, after consultations with industry representatives and European government officials. The TPM contains a surge-monitoring mechanism and strengthened price-monitoring procedures.

In the case of autos, Treasury participated in an interagency committee reviewing the 201 (escape clause) case under consideration by the USITC. In June 1980 the United Auto Workers filed a complaint with the USITC alleging that automobile imports have seriously injured the U.S. auto industry. The Ford Motor Co. later joined the complaint. The USITC announced on November 10, 1980, that imported automobiles were not the substantial cause of injury to the U.S. auto industry. The USITC will issue a formal report to the President November 24.

#### Export policy

The administration has taken several steps during the fiscal year to strengthen U.S. export performance.<sup>2</sup> This included a reorganization of the international trade functions within the executive branch, increased funding for export financing, and support for legislation to stimulate the formation of export trading companies (ETC's).

Treasury played an important role in the development of legislation to facilitate the formation of ETC's to assist exports by small and medium-size U.S. firms. Only a few ETC's exist now, because of the high marginal cost of developing foreign markets. The Senate unanimously passed legislation (S. 2718) which would permit banks to invest in ETC's, subject to specific limits and safeguard provisions, and would provide for immunity from antitrust for trading activities certified by the Department of Commerce. [The bill subsequently died in the House, however.]

<sup>1</sup> See exhibit 80.

<sup>2</sup> See exhibits 58 and 80.



Treasury was active in the formulation of two administration studies—"Study of U.S. Competitiveness" and "Export Promotion Functions and Potential Export Disincentives"—mandated by Congress in section 1110 of the Trade Agreements Act of 1979. These reports were undertaken to examine the competitiveness of U.S. goods in world markets and to highlight areas where the administration of U.S. export policy could be improved.

The above work was closely coordinated with that of the President's Export Council (PEC), of which Secretary Miller is a member. The PEC has brought together leaders in the private sector with senior administration officials and Members of Congress to examine the ways and means to improve U.S. export performance through administrative reforms, tax restructuring, and expanded export programs.

#### East-West trade

The U.S.-China Joint Economic Committee, established in early 1979, met in Washington in September 1980 to review progress in our bilateral trade and economic relations. Vice Premier Bo Yibo led the Chinese delegation, assisted by Finance Minister Wang Bingqian. Treasury Secretary Miller led the U.S. delegation.<sup>3</sup>

The main subjects covered in these discussions were: Business facilitation, finance, investment, and trade policy. The culmination of the session was Vice Premier Bo's meeting with President Carter and the signing of bilateral agreements in the fields of textiles, civil aviation, maritime affairs, and consular matters. The tone of the meeting was positive, with both sides underscoring the importance each attached to increased economic cooperation. The progress made in the course of normalizing economic relations is demonstrated by the expansion of trade from \$1.2 billion in 1978 to an estimated \$4 billion in 1980.<sup>4</sup>

The United States has encouraged active Chinese participation in the activities of international organizations such as the World Bank and the International Monetary Fund (IMF). With the participation of the People's Republic of China in the IMF, China's quota was raised from SDR 550 million to SDR 1,200 million. In addition, the number of Executive Board seats was raised by one (to 22) to accommodate the election of a Chinese Executive Director at the 1980 annual meeting.

Bilateral trade and economic relations between the United States and the Soviet Union declined in 1980. In response to the Soviet invasion of Afghanistan, President Carter imposed a variety of economic sanctions against the U.S.S.R., including a partial embargo of U.S. agricultural products, tighter controls on high-technology goods, an embargo of Olympic-related equipment, an embargo on phosphate exports, and tighter controls on energy technology exports. In addition, the U.S.-U.S.S.R. Joint Commer-

<sup>3</sup> See exhibits 52 and 60.

<sup>4</sup> See exhibit 80.



cial Commission, scheduled to hold its eighth session in April 1980, was postponed indefinitely.

In July of 1980 the President recommended to Congress the extension of his authority to waive the restrictions contained in section 402 of the Trade Act of 1974, for another year. The continuation of the waiver authority allowed the bilateral trade agreements the United States has with Romania, Hungary, and China to remain in force. During the first 7 months of 1980 U.S. trade with Eastern Europe increased by 29 percent compared with last year.

#### Export credits

*Industrial products.*—Under Treasury leadership, negotiations were launched early in 1980 to improve the International Arrangement on Export Credits. The launching of negotiations followed the completion of an interest rate study by Ingmar Wallen of Sweden. The Wallen Study emphasized the need to harmonize official export credit systems in order to reduce and eventually eliminate subsidization. The study suggested several possible modifications of the rigid interest rate structure of the present arrangement, including a differentiated rate system and a uniform moving matrix system.

During the June 1980 summit conference in Venice, the heads of state of the major industrial countries reaffirmed their commitment to reduce export credit competition. The Venice summit communique included a commitment by the participating countries to negotiate a mutually acceptable reform of the International Arrangement by December 1, 1980.<sup>5</sup> In related efforts, Treasury led U.S. delegations to meetings of the OECD Export Credits Group as well as to bilateral meetings with principal participants to the International Arrangement to discuss export credit policies.<sup>6</sup>

Until the Arrangement successfully reduces the extent to which participants engage in export credit subsidization, the administration will continue to press for increased funds for the Export-Import Bank (Eximbank) to match foreign competition.<sup>7</sup> The administration increased the Eximbank's direct loan and loan-equivalent authority in fiscal 1980 to \$5.1 billion. The direct loan budget was increased from \$3.75 billion in fiscal 1979 to \$4 billion in fiscal 1980; in addition, the administration arranged for further lending authority of \$1.1 billion for long-term, fixed-interest loans through the Private Export Funding Corporation.<sup>8</sup>

*Agricultural products.*—Treasury also provided intensive advice and assistance to the Agriculture Department during fiscal 1980 which aided in the transition of the Commodity Credit Corporation (CCC) from direct credit and noncommercial risk assurance programs in fiscal 1980 to guarantee programs in fiscal 1981, thereby providing incentives for greater private market participation in financing the export of U.S. agricultural goods. The smooth transition to private sources of financing was due in part to CCC's

<sup>5</sup> See exhibit 68.

<sup>6</sup> See exhibits 57 and 80.

<sup>7</sup> See exhibit 80.

<sup>8</sup> See exhibit 57.

previous decision—advised by Treasury—to supply loans at commercial rather than subsidized interest rates.

GSM-5 and other direct credit programs were allocated \$800 million of the Federal budget in fiscal 1980. The GSM-101 program, which provided assurances against noncommercial risks for U.S. agricultural exporters and financial institutions, operated under a \$1 billion ceiling set by CCC, to bring the total CCC budget for financing agricultural exports to \$1.8 billion in fiscal 1980. The GSM-5 and other direct credit programs were phased out at the close of fiscal 1980 in favor of the GSM-102 program for fiscal 1981, which will provide both commercial and noncommercial risk assurance to U.S. exporters and financial institutions without the need of Federal funding, except on a contingency basis.

*Foreign military sales.*—The U.S. Government provided approximately \$2 billion in foreign military sales credit financing to 25 countries as part of its security assistance program during fiscal 1980. The fiscal 1979 financing included \$3.7 billion for Egypt and Israel in connection with the Egyptian-Israeli Peace Treaty.

Treasury officials have become increasingly concerned over the growing tendency of industrialized countries to demand offsets in the form of countertrade, coproduction, direct investment, or mandatory technology transfers as a condition for purchasing major military systems. The principal Treasury concern is the increasing tendency of such transactions to spill over into the nondefense sector, adversely influencing the competitiveness, trade, employment, and tax revenues of the United States.

#### Investment developments

Treasury continued to take the leading role within the U.S. Government in guiding U.S. efforts to encourage international consideration of the problems associated with the use of investment incentives, disincentives, and performance requirements by governments and possible ways of dealing with them.<sup>9</sup> Treasury represented the U.S. Government in discussions of these issues in such international fora as the OECD and the Joint Development Committee of the International Monetary Fund and the World Bank.

Treasury Assistant Secretary Bergsten chaired a subgroup of the Joint Development Committee—the Task Force on Private Foreign Investment. This group consisted of delegates at the subministerial level from 12 major industrial and developing nations who met 6 times in the course of a year to discuss investment-related problems. The task force submitted a report in July 1980 which endorsed the objectives of seeking an international understanding to limit the adverse effects of investment incentives and of considering what further action was needed concerning performance requirements.<sup>10</sup> The report also recommended that the World Bank group undertake a study of these measures. At its annual meeting in September 1980, the full Develop-

<sup>9</sup> See exhibit 54.

<sup>10</sup> See exhibit 59.

ment Committee, which consists of the Secretary of the Treasury and Ministerial representatives of other IMF and International Bank for Reconstruction and Development (IBRD) member countries, referred favorably to these recommendations; the International Finance Corporation (IFC) is planning such a study.

The Committee on Foreign Investment in the United States (CFIUS), chaired by Assistant Secretary Bergsten, met periodically in fiscal 1980 to monitor the impact of foreign investment in the United States and to coordinate U.S. policy on such investment. Among the issues it discussed were State investment incentives and restrictions on foreign investment, Federal incentives, proposed investments by Royal Dutch/Shell in Belridge Oil Co. and Nippon Kokan KK in the Kaiser Steel Corp., and the report by the Committee on Government Operations concerning the adequacy of the Federal Reserve response to foreign investment in the United States. The CFIUS is also coordinating the administration response to this report.

Assistant Secretary Bergsten testified before a congressional subcommittee and presented the administration's views on the Reciprocity in Foreign Investment Act.<sup>11</sup> His testimony summarized U.S. policy toward direct investment and described the recent trends of foreign investment in the United States.

#### United States-Saudi Arabian Joint Commission on Economic Cooperation<sup>12</sup>

In November 1979, Secretary Miller visited Saudi Arabia. During that visit, he and Minister Abalkhail signed an extension of the original United States-Saudi Arabian Technical Cooperation Agreement for an additional 5 years to February 13, 1985. The Joint Commission met in Washington for its fifth annual session on April 1-2, 1980. The session reviewed the progress and accomplishments of the 19 project agreements involving almost total reimbursable funding. Over \$450 million has been deposited by the Saudi Arabian Government to date for the American technical assistance. Some of the session's highlights were the extension of the Statistics and Data Processing Agreement, one of the original project agreements, and the signing of the 20th and newest project agreement involving assistance to King Faisal University in Dammam and Hofuf, Saudi Arabia.

The focus of the Joint Commission's technical assistance effort will stress even more professional and technical manpower. This is consistent with the theme of Saudi Arabia's newest and third 5-year plan that emphasizes education and economic diversification over infrastructure. Major areas of Joint Commission concern involve agriculture and water research, national park management, vocational training, financial information analysis and dissemination, consumer protection, nationally sponsored scientific research, desalination research, solar energy research, highway system management, government auditing, customs administration and training, centralized gov-

<sup>11</sup> See exhibit 59.

<sup>12</sup> See exhibits 53, 55, and 56.



ernment supply management, national census and statistical analysis and computerization, agricultural loan administration, urban transportation systems, electrical services, and meteorological and arid lands studies.

There are presently over 200 American Joint Commission specialists and their families in residence in Saudi Arabia. Most of the specialists are in Riyadh, but some are in Jidda, Abha, Hofuf, and Dammam.

## Commodities and Natural Resources Policy

### International commodity developments

During fiscal 1980, negotiation of the Natural Rubber Agreement was completed and the United States signed and ratified it; negotiations on the Articles of Agreement for the Common Fund, a new international financial institution to facilitate the financing of international commodity agreements, were concluded; the ratification of the Sugar Agreement was completed; and new economic provisions of the Coffee Agreement were implemented. Negotiations of a new Tin Agreement and new Cocoa Agreement, both suspended in May 1980, were scheduled to be resumed in early fiscal 1981. Jute was marked as the first United Nations Conference on Trade and Development (UNCTAD) commodity to be considered for a nonstabilization ("other measures") agreement. Fiscal 1980 also saw the passage of U.S. ocean mining legislation and progress in the negotiation of a comprehensive Law of the Sea treaty.

*The Integrated Program for Commodities (IPC).*—The IPC, developed at UNCTAD IV in 1976 and reaffirmed at UNCTAD V in 1979, serves as a framework for international commodity discussions, for negotiation of intergovernmental agreements to stabilize commodity markets, and for establishment of the Common Fund to facilitate the financing of such agreements. In the U.S. view, market stability can best be achieved, and market efficiency can best be served, by commodity agreements based on buffer stocks large enough to function effectively.

*Common Fund.*—Articles of Agreement for the Common Fund were concluded in June of this year. The Articles specify that the Common Fund will have two separate accounts. The First Account will facilitate the financing of the buffer stocking operations of international commodity agreements associated with the Fund. The resources of the First Account will be derived primarily from the resources of associated commodity agreements, supplemented by up to \$400 million in capital contributed directly to the Fund by Common Fund members. The Second Account will finance commodity development measures, e.g., marketing, research and development, etc., and will be funded by voluntary contributions. The United States does not plan to contribute to the Second Account in the foreseeable future. An intergovernmental body, the Common Fund Preparatory Commission, will meet during fiscal 1981 to begin preparation of materials necessary for the operation of the Common Fund once it enters into force.



The completion of the Articles of Agreement represents the culmination of 4 years of intensive negotiations and represents a significant achievement in the North/South context. In these negotiations, the United States played a major role and was instrumental in ensuring that the Common Fund would be viable.

*Oceans policy.*—President Carter signed the Deep Seabed Hard Mineral Resources Act to promote the orderly development of the deep seabeds, pending the adoption of an international agreement. The legislation establishes a legal regime which will offer a stable investment climate for potential U.S. seabed miners. The legislation is fully consistent with U.S. objectives in negotiations for a comprehensive Law of the Sea treaty, since the domestic regime is designed as an interim measure until an acceptable treaty enters into force for the United States and precludes full-scale commercial production before January 1, 1988.

In 1980, the United Nations Conference on Law of the Sea produced an informal text of a draft convention. It was generally agreed that newly negotiated seabed mining texts on decisionmaking, finance, and final clauses be included in the draft convention, since they offered greater opportunity for ultimately achieving consensus on a comprehensive Law of the Sea treaty. The Conference is scheduled to resume in March 1981 to complete its work on remaining issues.

#### Commodity developments

*Copper.*—UNCTAD discussions on copper, which began in late 1976, have yet to advance to the stage where countries are prepared to negotiate an intergovernmental price stabilization agreement for copper. Some countries prefer a producer/consumer forum for collecting statistical data and preparing economic studies; others prefer a price-stabilizing agreement combining a small buffer stock and some form of supply control. The United States has sought to introduce the concept of a buffer stock large enough (at least 1 million metric tons) to stabilize the world copper market effectively without a need to resort to other economic measures such as export or production controls. Other countries have shown little interest in the U.S. concept. Preparatory meetings in October 1979 and March 1980 did not produce an agreed basis for negotiating an intergovernmental arrangement in any of these forms.

*Tin.*—In April-May 1980, the United States and other members of the Fifth International Tin Agreement began the negotiation of a sixth agreement, which would enter into effect in July 1981. The United States sought to enlarge the size of the tin agreement's buffer stock from the current 40,000 metric tons to 70,000 metric tons, to assure commitments by member governments to finance the full amount of the buffer stock, and to eliminate export controls. However, other major participants were opposed to increased stocking and financing obligations and to the elimination of export controls. The April-May negotiating session ended inconclusively, given this

wide difference of views. Participants met informally in July and September to develop a common basis for renewing negotiations at the end of the year.

*Rubber.*—Negotiation of the International Rubber Agreement concluded in early October 1979. The agreement was open for signature from January 2 to June 30, 1980, and was to enter into force on October 1, 1980. The United States signed the agreement in April 1980, and the Senate ratified the agreement in May.<sup>13</sup> In August, the House passed an appropriation of \$88 million— to cover U.S. obligations for financing the agreement's buffer stock—the full amount requested by the administration. In September, the Senate Committee on Appropriations passed an appropriation of \$45 million. Pending resolution of this difference in conference, the administration announced in September that the United States planned to join the rubber agreement provisionally for 18 months. This action allows the rubber agreement to enter into force provisionally since signatory members' total share of world trade in natural rubber now exceeds the 65-percent level required for the agreement to enter provisionally into force. The terms of provisional entry into force do not require a U.S. financial commitment during the 18-month period of provisional U.S. membership.

*Coffee.*—At the annual meeting of the Council held in September, consuming countries, led by the United States, were finally successful in getting producers to cease their market intervention. As part of the settlement, the economic provisions, i.e., export quotas, of the existing coffee agreement will be put into effect to defend an agreed price range. When the economic provisions are activated, the U.S. participation will be contingent on the passage of implementing legislation by Congress.

*Cocoa.*—On March 31, 1980, the cocoa agreement, of which the United States was not a member, expired despite several attempts at renegotiation. Since this agreement was viewed as a possible adjunct to the Common Fund, UNCTAD Secretary General Corea has attempted to reconcile the differences between producers and consumers. The major hurdle to a new agreement is the buffer stock's lower intervention price which producers want set at a level consumers feel is not compatible with the cocoa supply and price outlook over the next few years.

*Sugar.*—During the year, the sugar agreement was ratified and the necessary implementing legislation was signed by the President. This enabled the United States to carry out its obligations which called for a limitation on imports under certain conditions and to verify collection by the International Sugar Agreement of the fee on sugar traded among members. A drastic shift in the world supply/demand situation in the latter half of the fiscal year was beyond the capability of the agreement's price mechanism. Stocks released in February, as prices rose past the trigger points, helped moderate prices. News of poor crops developing in Cuba, the Soviet Union, South Africa, and Thailand, and Brazil's decision to use sugarcane to make fuel alcohol created

<sup>13</sup> See exhibit 61.

an extremely tight supply outlook for the 1981-82 crop year, and prices which began fiscal 1980 at around 10 cents a pound escalated to almost 40 cents by the fiscal year's end.

*Other commodities.*—The UNCTAD jute discussions, which had been characterized by a lack of progress because of the contentious issue of price stabilization, finally led to an intergovernmental decision to negotiate a nonstabilization ("other measures") agreement. While disagreements over the need for, and the feasibility of, a price stabilization arrangement for cotton continue to impede progress in UNCTAD talks, discussions are proceeding, albeit slowly, in other fora on nonstabilization measures.

*Grain agreements.*—Another facet of U.S. commodity policy involves the pursuit of arrangements contributing to greater world food security and lessening the impact of grain price volatility on the U.S. economy. One approach toward this objective was the negotiation of bilateral grain sales agreements. On October 21, 1980, the United States signed a 4-year grain sales agreement with the People's Republic of China calling for annual purchases of 6-8 million tons, most of which will be wheat. But the other major bilateral agreement, with the U.S.S.R., suffered a setback when the United States restricted sales to the Soviet Union under the agreement. Grain sales were limited to the 8-million-ton minimum permissible quantity by President Carter in response to Soviet aggression in Afghanistan.

#### World oil market

In contrast to the tight supply situation and sharp price increases experienced during fiscal 1979, the world oil market was somewhat less volatile in fiscal 1980. As a result of recession and improved conservation, OECD consumption at the end of fiscal 1980 was running about 5 percent below the previous year's level. U.S. oil use during the first three quarters of 1980 averaged about 16.8 mmb/d, down 9 percent from 1979 levels. Oil supplies also declined as producers cut back output in the face of slack demand. As a result, free world crude output in August 1980 was 3½ mmb/d below end-1979 levels. Nevertheless, supply consistently exceeded consumption, by perhaps as much as 2 mmb/d towards the end of the fiscal year. This surplus permitted the accumulation of world stocks considerably in excess of the levels needed for normal operations and seasonal adjustments.

Despite the adequacy of supplies on world markets, producers were able to substantially increase their prices during the year. The average official Organization of Petroleum Exporting Countries (OPEC) price rose from \$20.14 in September 1979 to \$31.63 in August 1980, an increase of over 50 percent. Individual prices diverged widely from this average, ranging from about \$30-\$39/bbl in September 1980, including premiums added by some producers. While OPEC made some progress in reunifying prices, hopes for a rapid agreement were dashed by the onset of the Iran-Iraq hostilities in late September 1980.



These OPEC price increases once more were a major factor depressing economic progress and intensifying inflationary pressures in the United States and elsewhere. They also led to a sharp deterioration in the payments position of both OECD and nonoil developing countries and sharp increases in OPEC country surpluses.

#### Energy policy<sup>14</sup>

The administration has given high priority to the development of a national energy program aimed at reducing U.S. dependence on imported oil. Major elements of President Carter's July 1979 energy program became effective during fiscal 1980. In particular, the June 1980 Energy Security Act authorized the establishment of the Synthetic Fuels Corporation to stimulate synfuels production. The legislation calls for synfuels production of 500,000 b/d of oil equivalent by 1987 and 2 mmb/d of oil equivalent by 1992. The Corporation will be financed from proceeds of the windfall profit tax which became effective March 1, 1980.

During the year, Treasury policies and programs were particularly concentrated on the effects of OPEC price and supply decisions on the U.S. economy, demand restraint and alternative energy production in the context of our International Energy Agency and Venice economic summit<sup>15</sup> commitments, and energy exploration and development in developing countries. Treasury officials engaged in international and bilateral discussions on energy and responded to numerous invitations by Congress and the public to speak on a wide range of energy issues.

#### Venice economic summit

Energy was the key topic at the June 1980 Venice economic summit. The summit emphasized longer run programs to conserve and develop alternative energy sources during the 1980's. Regarding conservation, the participants agreed to various measures including limiting oil-fired generating capacity, fiscal and financial incentives as well as insulation standards to encourage oil-saving investments in the industrial and residential/commercial sectors, and increased auto fuel efficiency. Regarding production, the summit agreed to develop policies for the increased production of coal, nuclear, synthetic, and renewable energy resources so as to achieve savings of 15–20 mmb/d of oil by 1990. The summit expressed the view that these and other measures should result in a 0.6 energy/gnp growth ratio and reduce the oil share in total energy demand to 40 percent by 1990.

The summit also asked the World Bank to study the adequacy of existing energy development programs and resources, to consider means, including the establishment of an affiliate or facility, by which it might increase and improve its energy lending programs, and to explore these possibilities with

<sup>14</sup> See exhibit 26.

<sup>15</sup> See exhibit 68.



both oil-exporting and industrial countries. The World Bank is currently undertaking such a study.

#### International Energy Agency (IEA)

The IEA continues to serve as an important vehicle for the coordination of the international energy policies of 21 industrialized oil-consuming member countries. IEA efforts have been directed at reducing dependence upon imported oil through conservation, accelerating development of indigenous resources, and furthering research and development. In addition, the IEA has developed methods to restrain demand and share existing supplies in the case of a supply emergency situation. The major achievement of the IEA during fiscal 1980 was the setting of industrial country oil import targets for 1980 and 1985 and the establishment of a system by which annual yardsticks (i.e., estimates of individual countries' oil requirements) could be transformed into politically binding ceilings in the case of a short-term market disruption. A system for governmental consultations on stock policies was also established. Most recently, in response to the oil market disruption associated with the Iran-Iraq hostilities, the IEA agreed to measures to avoid abnormal spot market purchases and to draw down stocks to the extent necessary to balance the market in the fourth quarter. Treasury participated in the meetings of the Governing Board and several subordinate groups.

*Standing Group on Emergency Questions (SEQ).*—The SEQ reviewed the progress of member countries in adopting demand restraint measures, prepared the data base to be used in determining oil import targets, and proposed actions to discourage the purchase of high-priced spot oil by member countries. The SEQ also worked out final details on a Dispute Settlement Center, whose charter was approved by the IEA Governing Board in July. The Settlement Center will adjudicate pricing disputes which may arise during implementation of IEA's emergency oil supply sharing system.

*Standing Group on Oil Markets (SOM).*—The SOM studied the changing structure of the world oil market and its implications in the market. It worked out a system for consultations within the IEA and between governments and the oil industry on stock policies. It is considering the possibility of cooperative stock management among member countries in order to prevent a runup in spot prices during a supply disruption not severe enough to trigger the formal IEA oil sharing program. It was instrumental in the establishment of a registration system for crude oil imports, adopted November 1, 1979, and a register for products, adopted in spring 1980.

*Standing Group on Long-Term Cooperation (SLT).*—The Standing Group reviewed the energy policies of individual countries and came to the conclusion that present programs and potential oil supplies were inadequate to maintain balance in the oil market in the longer run—leading to a May 1980 Ministerial decision that IEA countries as a group should substantially undershoot the existing 1985 group objective (26.2 mb/d of oil imports). The

Group also worked out Principles for IEA Action on Coal and procedures for review of IEA countries' coal policies—also adopted at the May Ministerial meeting. Finally, it undertook a study for the Governing Board on demand management in the 1980's in order to assess the long-term structural changes needed by the IEA economies.

#### Relations with producing countries

In relations with the producing countries, U.S. efforts have focused on obtaining a secure supply of oil at a reasonable price. More generally, we are concerned with developing a solution to the global energy problem which will be acceptable to both producing and consuming countries. At the Venice summit, the industrialized countries once again indicated their willingness to engage in constructive energy discussions with the producing countries.

It appears that OPEC countries, within the context of their long-term strategy, are considering proposals for an oil price indexation scheme, increased assistance to the developing countries, and energy discussions with the industrialized countries.

#### Energy development in developing countries

In its relations with the developing countries, the United States has been guided by a belief that reducing the dependence of developing countries on expensive oil imports will both further their development and improve the world energy balance. In pursuit of these objectives, the United States took further steps during fiscal 1980 to help the LDC's develop their own energy resources. As noted above, the Venice economic summit requested the World Bank to study means by which it could improve and increase its energy lending. The United States also strongly supports and is an active participant in preparations for the August 1981 U.N. Conference on New and Renewable Sources of Energy.

In addition to these multilateral efforts, the United States encourages LDC energy development through bilateral cooperation and assistance programs. The Department of Energy is helping LDC's to determine their energy needs and available energy alternatives. The Agency for International Development and State Department have programs to assist the LDC's in developing renewable energy technologies. The Overseas Private Investment Corporation provides insurance coverage for energy projects.

### International Monetary Affairs

#### World economic and financial developments

*The world economy.*—A substantial slowdown in world economic growth, together with an acceleration in inflation, occurred during fiscal 1980. Developed and developing countries alike experienced a weakening of the foundations for sustained, noninflationary real growth which had been gradually rebuilt after the "stagflation" experience of 1974/75. By the end of

September 1980, however, the worst of the slowdown in growth and acceleration of inflation appeared to have passed. The outlook was that a moderate recovery and gradual reduction in inflation would be attained in fiscal 1981.

The effects of higher oil costs heavily influenced the path of economic output throughout the period. After strong growth in the first quarter of 1980, virtually no real growth took place in industrial countries as a whole during the rest of the calendar year. Several experienced negative growth rates in the second quarter, and a few in the third as well. A modest recovery was expected during the fourth quarter.

The sharp slowdown in growth during the middle two quarters of 1980 was likely to result in much slower growth for the year as a whole than was recorded in 1979. Latest data suggest that GNP in the OECD area in total expanded by slightly more than 1 percent during calendar 1980, compared with 1979's average 3.3 percent real GNP growth. As a result of this well-below potential growth rate, unemployment rates rose throughout the industrial world. Among the major industrial countries, however, patterns of slowing and recovery were sufficiently varied, both in timing and intensity, that only in a very loose sense could 1980 be characterized as a synchronized downturn, such as occurred in 1974/75.

Real growth in the major nonoil developing countries as a group rose marginally to about 5.5 percent in calendar 1980, as compared with 5.2 percent in 1979, but is likely to slow in 1981 as external financing pressures induce a more modest pace of economic activity in some of the larger developing countries.

By late spring 1980, average annual inflation rates within the OECD area, as measured by cost-of-living indices, peaked in the 14-percent range. Modest improvements were recorded subsequently, with the average rate having fallen to 12.3 percent by October. The inflation rate for the calendar year as a whole, however, was likely to be about 12 percent, as compared with the 9 percent recorded in 1979. Among the major industrial countries, the highest rates of inflation were observed in Italy and the United Kingdom (22 percent), and the lowest in Germany (6 percent) during the spring.

Monetary policies were tightened substantially during fiscal 1980 in most OECD member countries. This is in marked contrast to the 1974/75 experience, when many governments attempted to make up for the real income losses due to the oil price increases by following expansionary monetary and fiscal policies. Targets for monetary aggregates in the major countries have been either lowered or left unchanged, and controls on credit expansion have in most cases been stiffened. On a year-over-year basis money supply growth in most major countries showed a definite deceleration during fiscal 1980. The interest rate declines which occurred were due more to a slackening of credit demand as output growth slowed than to an easing of monetary policy.



In addition, fiscal policy in most of the major countries was somewhat more restrictive in 1980 than in 1979. As a result of this nonaccommodative monetary and fiscal policy stance, the inflationary effects of the 1978-79 oil shock should be somewhat smaller than those following the 1973-74 oil price increases, whether in the form of sympathetic increases in prices of petroleum substitutes or pressures on wages and prices.

Non-oil-exporting developing countries also face serious inflation problems. For this group of nations in the aggregate, consumer price increases probably reached 38 percent during calendar 1980, a sizable increase from the average 30-percent increase of 1979. The major developing countries—largely reliant on private external finance—experienced substantially more rapid inflation, in excess of 50 percent, in 1980.

*The international balance of payments situation.*—Global payments imbalances were substantially larger during calendar 1980 than in 1979, with only marginal improvement expected in 1981. The OPEC current account surplus is estimated to have totaled slightly more than \$100 billion in 1980 (versus \$59 billion in 1979), and is expected to decline only moderately in 1981. The OECD area experienced a sharp deterioration in its external position, with the combined current account deficit for OECD countries estimated at \$74 billion (versus \$36 billion in 1979). The aggregate deficit of the nonoil developing countries rose by approximately \$21 billion in 1980, to a total of \$61 billion (*after* receipt of \$18 billion in official transfers). Centrally planned economies experienced about the same combined deficit in 1980 (about \$8 billion) as in 1979.

About half of the deterioration in the current account position of the OECD area occurred in the group of seven major industrial countries, whose combined deficit position is estimated to have increased from \$17 billion in 1979 to \$37 billion in 1980. The U.S. current account showed a small surplus in 1980, following approximate balance in 1979, while Japan and Germany experienced larger deficits than they recorded in 1979. However, the aggregate deficit of this group of countries is likely to decline substantially in 1981 as a consequence of slower growth and reduced oil imports. All of these countries have major access to credit and should have few problems arranging sufficient external financing.

Among the smaller industrial countries, aggregate current account balances are estimated to have deteriorated by some \$18 billion in 1980, from \$18 billion in 1979 to almost \$37 billion in 1980. The group of “privately financed” developing countries—those relying primarily on private rather than official financing—probably accounted for more than half of the \$61 billion aggregate current account deficits of non-oil-exporting developing countries. Some of these countries—both the smaller industrial countries and developing nations—may encounter growing financing problems and pressures to strengthen their external positions at an early stage in 1981.

*International bank lending, the Eurocurrency market, and official reserve diversification.*—Private banks were able to provide the major part of the



increased international financing sought in 1979 as a result of increased payments imbalances, continued accumulation of reserves by some deficit countries, further rapid growth in nominal terms of world trade, and a tightening of credit terms for purchases of oil. New lending, net of repayments and excluding purely interbank activity, increased by about \$130 billion, representing a rate of increase about the same as the 25-percent increase recorded in 1978.

Despite a further enlargement of current account imbalances, new private bank lending in 1980 did not rise much, according to data available through September. This trend, particularly marked for developing countries, reflects in part the cessation or reversal of reserve accumulation by many borrowing countries—and thus the removal of a major factor in their “demand” for external borrowing. The absence of the United States as a major international borrower in 1980 also contributed to the trend. (The pace of publicized gross medium- and long-term bank credits actually declined from the 1979 level. However, this is not a good indicator of overall net banking flows, in part because it does not reflect changes in the level of short-term credits.)

Due in large part to unsettled market conditions, financing raised through external bond issues in 1980 rose only slightly over the level of 1979, despite the concentration of current account deficits in large OECD countries whose residents traditionally rely more heavily on this form of finance than do those of other countries.

As noted in the preceding Annual Report, the United States helped to initiate a study in central bank channels of a number of questions concerning international bank lending and particularly the Eurocurrency market. This study was completed in spring 1980 and has resulted in a more formal monitoring of trends in international lending and in further work on development of better data on banks’ maturity transformation and on reduction of differences in competitive conditions as between domestic and Eurocurrency markets.

Private banks’ deposit liabilities include placements by governments of the bulk of their foreign exchange reserves. Most of these reserves have been and continue to be held in dollars. As reported by banks in most of the financial centers, the amount of bank deposits and selected securities comprising official reserves which are denominated in dollars rose \$56 billion from end-1977 to September 1980. Although there has been some decline during this period in the proportion of total foreign exchange reserves which are held in dollars, dollar holdings still accounted for over 76 percent of the total as of September 1980.

*Foreign exchange market developments and operations.*—Exchange markets accommodated, without serious and prolonged periods of disorder, numerous political and economic strains, including the seizure of American hostages in Iran, the Soviet invasion of Afghanistan, unprecedented speculation in gold and other precious metals, further inflationary shocks from OPEC oil price increases and supply reductions, and the outbreak of war between Iran and

Iraq. The maintenance of broad market stability and the relatively firm position of the dollar reflected in particular a strengthening of the U.S. current account and a deterioration of the current account positions of other major countries, U.S. monetary restraint, and continued close cooperation between U.S. and major foreign monetary authorities in the conduct of exchange market operations.

On balance, the dollar appreciated by 1 percent during the fiscal year on a trade-weighted basis against other OECD currencies. The dollar appreciated by 4 percent against the German mark and to a lesser extent against most of other currencies of the European Monetary System (EMS), by 6 percent against the Swiss franc, and by 1 percent against the Canadian dollar; the dollar depreciated by 6 percent against the Japanese yen and by 8 percent against United Kingdom sterling.

At the beginning of the fiscal year, market psychology toward the dollar was bearish. The dollar was experiencing generalized selling pressure and had depreciated to near its pre-November 1978 lows in terms of the German mark. Successive OPEC oil price increases had aggravated inflationary pressures in the U.S. economy and impeded improvement in the trade account. Economic activity in the United States remained robust, contributing to demand for imports. Moreover, authorities in major foreign countries were viewed as willing to adopt relatively more stringent financial policies to combat inflation. This perception, coupled with events associated with the end-September realignment of EMS currency values, generated substantial speculative demand for German marks. Gold and other precious metals markets experienced a wave of speculation, reflecting in part a surge of inflationary expectations.

Against this background, following an early October meeting in Hamburg, Secretary Miller, Federal Reserve Chairman Volcker, and German Chancellor Schmidt reiterated their resolve to combat unwarranted as well as erratic movements in the foreign exchange markets, pointing out that the necessary interventions would be carried out promptly and in close cooperation. On October 6, the Federal Reserve announced a change in its domestic money market operating procedures to emphasize control over the level of reserves in the banking system rather than the targeting of the Federal funds rate. In addition, the discount rate was raised from 11 percent to 12 percent. The Treasury announced that it would issue additional German mark-denominated securities in the German capital market, thereby increasing U.S. resources for foreign exchange market operations.

Also during October, the Treasury announced that it would no longer hold regular monthly gold auctions but would pursue a more flexible gold sales program to help deter the speculative disturbances in the gold market which had contributed to instability in other commodity markets and the exchange markets.<sup>16</sup> Henceforth, sales would be subject to variations in amounts and

<sup>16</sup> See exhibit 63.

timing, thereby increasing the uncertainties and risks associated with gold speculation. In accordance with this approach, the Treasury auctioned 1.25 million ounces of gold on November 1. No further bullion sales were conducted during the fiscal year.

The measures announced in October contributed significantly to the restoration of order in the exchange markets. The ensuing movement in interest rate differentials in favor of dollar-denominated investments and the perception that U.S. authorities were more aggressively pursuing anti-inflationary policies calmed markets and generated demand for dollars.<sup>17</sup>

The dollar eased again in November, however, and continued to experience pressures through early January 1980. During this period, the market was influenced by political uncertainties surrounding the situations in Iran and Afghanistan, apprehensions concerning the economic ramifications of further OPEC oil price increases, and disappointing U.S. trade and price performance. In addition, sharp increases in certain foreign interest rates more than offset the earlier rise in U.S. interest rates, attracting funds into foreign currency investments.

Amid these developments, the seizure of American hostages in Iran on November 4 and Iranian threats to withdraw their assets from U.S. banks exacerbated uncertainties in the exchange market, though the market responded favorably to the President's decision to cease petroleum imports from Iran and to freeze official Iranian assets.

In December, apprehensions regarding the inflationary repercussions of another bout of oil price increases triggered further generalized sales of dollars. As the dollar again declined to near its pre-November 1978 lows in terms of the German mark, the U.S. and German authorities intervened to maintain orderly conditions in the exchange markets.

In the period of relatively quiet market conditions that had prevailed during October, the Treasury and Federal Reserve were able to purchase foreign currencies to restore balances and repay swap indebtedness. Market operations in support of the dollar resumed in November and continued periodically in December and January. Nevertheless, over the October-December period as a whole, the U.S. authorities made net purchases of foreign currencies totaling \$210 million. The dollar appreciated by about 1½ percent on a trade-weighted basis against other OECD currencies during this period; among individual currencies, the largest movements were dollar appreciations of about 7 percent against the Japanese yen and 4 percent against the Swiss franc.

As the new calendar year began, exchange markets were extremely uneasy in light of political uncertainties surrounding the Soviet invasion of Afghanistan and the ensuing sharp surge in gold and other precious metals prices. As the month progressed, however, the market's apprehensions receded.

<sup>17</sup> See exhibit 64.



On February 15, the Federal Reserve raised the discount rate from 12 to 13 percent in light of continued large expansion in monetary aggregates, heavy credit demands, and acceleration in inflationary expectations. U.S. money market rate increases sharply exceeded those occurring in major foreign centers, thereby increasing interest rate differentials in favor of the dollar. As the dollar appreciated, commercial leads and lags, which had been adverse in 1979 in anticipation of dollar depreciation, were reversed.

Demand for dollars accelerated in mid-March through early April, following the President's announcement of further anti-inflationary measures geared toward reduction of the Federal budget deficit and curtailing oil imports. For its part, the Federal Reserve announced a series of measures under the authority of the Credit Control Act of 1969.

During January–March, U.S. and foreign authorities conducted large-scale foreign exchange operations to counter disorderly trading conditions as the dollar appreciated. The Treasury and Federal Reserve made net purchases of \$4.5 billion of foreign currencies. The Federal Reserve was able to repay in full its swap commitments and also purchased \$217 million equivalent of Japanese yen, in cooperation with the Japanese authorities. U.S. foreign exchange reserves were also augmented through the issuance of \$2.3 billion equivalent of German mark-denominated U.S. Treasury securities in the German market in November 1979 and January 1980. During January–March, the dollar appreciated by over 5 percent on a trade-weighted basis against other OECD currencies, rising against all major foreign currencies except the Japanese yen.

Between early April and mid-July the dollar depreciated largely in response to a sharp decline in U.S. interest rates. The decline in interest rates reflected an abrupt reversal in U.S. economic conditions led by a sharp retrenchment in consumer expenditures. As credit demands slackened and the narrowly defined money supply contracted to well below the lower end of the Federal Reserve's target band for growth in monetary aggregates, the decline in interest rates gained momentum. The depreciation of the dollar during this period, though relatively large—the dollar declined by nearly 12 percent against the German mark and by 9 percent on a trade-weighted basis in terms of OECD currencies—did not, however, generate substantial tensions on the exchanges. In part, the markets were influenced by reports of substantial improvement in the U.S. trade position and by somewhat reduced inflationary expectations. U.S. and foreign monetary authorities intervened in the market, forcefully at times, to steady trading conditions. During early April–mid-July, the Treasury and Federal Reserve made net sales of \$1.9 billion equivalent of German marks, \$264 million equivalent of Swiss francs, and \$127 million equivalent of French francs.

In July, U.S. monetary aggregates and credit demands expanded, and U.S. interest rates rose. The upward movement in interest rates was further propelled by release of indicators showing a greater than expected resurgence in the level of U.S. economic activity. Market sentiment was also affected by



a presumption that interest rates in major foreign countries would tend to decline.

Given the more favorable outlook for U.S. trade performance, and with interest rate differentials again moving in favor of dollar placements, demand for dollars reemerged. Though portfolio diversification sales of dollars were reported from time to time, the dollar appreciated in fairly steady exchange market activity through the remainder of the fiscal year. Toward the end of the period, flows into dollars accelerated as U.S. interest rates increased further, and the Federal Reserve raised its discount rate from 10 to 11 percent to contain the resurgence in the growth of the money supply.

From mid-July to the close of the period under review, the Treasury and Federal Reserve made net purchases of \$1.6 billion of foreign currencies. The dollar appreciated by 1 percent on a trade-weighted basis against other OECD currencies, rising by 4 percent against the German mark while declining by 1 percent against United Kingdom sterling and by 4 percent against the yen.

During the fiscal year, the issuance of \$2,287 million equivalent of German mark-denominated securities in the German market increased outstanding Treasury foreign-currency-denominated securities to \$6,437 million equivalent. At the end of the period, the general account of the Treasury had a net translation liability, less profits realized, associated with these securities totaling \$48 million.

#### Gold market developments

Gold prices moved over a wide range during the fiscal year, often in volatile trading, influenced by unsettled conditions in the Mideast and the effects of further oil price increases on worldwide inflation.

The price of gold had been bid up from around \$330 per fine troy ounce in early September 1979 to as high as \$425 per ounce in early October. The seizure of U.S. hostages in Iran further unsettled the markets in November. This factor, coupled with reactions to the Soviet invasion of Afghanistan in December, stimulated a wave of speculative panic in the precious metals markets in early January, in which gold prices reached a high of about \$850 per ounce. The price of gold then fell precipitously, reflecting in part the sharp increase in U.S. interest rates, and reached a low of \$475 per ounce in March. Prices increased to over \$600 in June and fluctuated rather widely over the remainder of the fiscal year, closing the year at about \$670 per ounce.

During the fiscal year, the Treasury sold a total of 2 million ounces of gold bullion in public auctions on October 16 and November 1, 1979, at a total value of \$759 million. Pursuant to the American Arts Gold Medallion Act of 1978, the Treasury commenced public sales of half-ounce and 1-ounce gold medallions on July 15, 1980. At the close of the fiscal year, medallions containing 259,000 fine ounces of gold had been sold, at a total value of \$165 million.

**International monetary arrangements<sup>18</sup>**

During fiscal 1980, the International Monetary Fund took a number of significant steps which will allow it to play a potentially major role in the financing and adjustment of current balance of payments disequilibria. The Fund also adopted important measures to strengthen its surveillance over the global economy and to promote the role of the special drawing right (SDR) in the international monetary system. These efforts were strongly supported and encouraged by the United States.

**Meeting official balance of payments financing needs**

The oil price increases of 1979 and 1980 led to large new payments imbalances and financing requirements.<sup>19</sup> While private capital markets will continue to provide the bulk of the financing required by deficit countries, the international community agreed that in present world economic circumstances the IMF should be prepared to play a larger role in the financing and adjustment of payments imbalances. The Secretary of the Treasury, at the 1980 IMF/IBRD annual meetings, described the challenge before the Fund: "to encourage the appropriate blend of adjustment and financing by member nations and to facilitate forms of adjustment and financing most supportive of a strong world economy."<sup>20</sup>

During the annual meetings, the Interim Committee endorsed a number of measures developed in the Executive Board to allow the Fund to play an expanded role in the current international economic environment.<sup>21</sup> Specifically, it was determined that:

- Members' access to IMF resources should be increased substantially in recognition of larger balance of payments financing requirements. Compared with the 100 percent of quota permitted only a few years ago, members will now be able to obtain up to 200 percent of quota annually for 3 years, or a total of 600 percent, in support of appropriate adjustment programs.
- Periods of adjustment associated with IMF-supported programs should be lengthened, reflecting the structural nature of changes in members' economies required by the new world energy situation. The IMF is now prepared to enter into successive 1-year programs covering several years.
- Greater emphasis should be placed on "supply-side" considerations in IMF programs, to stimulate the investment and productivity growth needed for successful structural adjustment. Although the Fund will work closely with the World Bank, particularly in the context of the Bank's new structural adjustment and energy lending programs, it will continue its traditional focus on macroeconomic policies in designing adjustment programs.

<sup>18</sup> See exhibits 62, 66, and 69.

<sup>19</sup> See exhibit 67.

<sup>20</sup> See exhibit 71.

<sup>21</sup> See exhibit 70.

- An interest subsidy account should be established for low-income developing countries that use the IMF's highest cost financing. The subsidy would be designed to reduce costs of loans from the Supplementary Financing Facility by up to 3 percentage points, and would be financed primarily from repayments of trust fund loans plus any voluntary contributions received from member countries.

Gross drawings on IMF resources amounted to SDR 3.1 billion in fiscal 1980, compared with SDR 4 billion in fiscal 1979—when the large U.S. reserve tranche drawing in November 1978 increased the figure by SDR 2.3 billion. Drawings on the IMF's more *conditional* resources (i.e., excluding reserve tranche drawings) nearly doubled from SDR 1.45 billion in fiscal 1979 to SDR 2.77 billion in fiscal 1980.

The IMF gold sales program, initiated in 1976, was completed in 1980. The IMF-administered trust fund made two disbursements of loans in 1980 to 50 of the poorest developing countries for a total of \$1,864 million. The final disbursement under the trust fund loan program was scheduled for spring 1981.

*IMF surveillance.*—The United States strongly supports an enhanced IMF role in surveillance over members' exchange rate policies and the balance of payments adjustment process more generally. As noted in previous Annual Reports, the IMF has adopted principles for the guidance of members in conducting exchange rate policy, and procedures and criteria for use by the Fund in assessing members' policies.

To further strengthen the Fund's surveillance role, the United States has advanced several proposals:

- The policies and performance of individual countries should be assessed by the IMF against a broadly agreed global economic framework.
- To promote greater symmetry of adjustment responsibilities, the Fund should seek adjustment policy statements and analyses from any country experiencing a large payments imbalance, whether surplus or deficit.
- The Managing Director should be permitted to take the initiative in consulting members where he has concerns about the appropriateness of their policies.
- The Fund's surveillance should be extended to the financing of payments imbalances including, for example, the size of borrowing and the placement of financial surpluses.

Implementation of these proposals will considerably enhance the IMF's surveillance over international liquidity as well as promote a more symmetrical and effective global adjustment process.

*Financing IMF activities.*—Members' quotas are central to all IMF operations. Among other things, they provide the permanent financial resources of the organization, are the basis for determining the amount of financing a member can obtain from the IMF, determine members' voting power, and



serve as the distributional basis for SDR allocations. Quotas are reviewed periodically in relation to the growth of world economic activity and international transactions, and the scale of payments imbalances and prospective financing needs. Despite four general increases in the past, quotas have fallen to about 4 percent of annual world imports, compared with 8–12 percent during the 1960's. In response, IMF members agreed in December 1978 to increase quotas by 50 percent to about SDR 58 billion. [The increase became effective in early fiscal 1981.]

In late fiscal 1980 the President signed legislation authorizing a 50-percent increase in the U.S. quota, from SDR 8,405 million to SDR 12,607.5 million. [A bill appropriating the full amount of the new subscription was subsequently enacted and the United States subscribed its quota increase on December 20, 1980.] As transfers of dollars to the IMF under the U.S. quota subscription are fully and simultaneously offset by U.S. receipt of a reserve asset in the IMF, payment of the quota subscription does not affect net budget outlays or the Federal budget deficit.<sup>22</sup>

Following this quota increase, the IMF will be in a reasonably strong position to meet official balance of payments financing needs. However, given the growth in demand for IMF resources during the course of fiscal 1980, the likely persistence of large payments imbalances, and the steps that have been taken to expand access to Fund resources, the Fund's liquidity could become strained in the next few years. Therefore, the IMF, with strong U.S. support, began exploring in 1980 the possibility of further borrowing, from both official and private sources, to supplement its resources.

*Special drawing rights.*—The United States believes that development of the SDR as a major monetary instrument can contribute to the orderly evolution and stability of the international monetary system, and has supported a number of measures taken by the Fund in 1980 to enhance the role of the SDR.

The most important decision taken was to unify and simplify (as of January 1981) the "currency baskets" used to calculate the value of, and interest rate on, the SDR. Before this modification, a basket composed of 16 currencies was used to value the SDR on a daily basis, and a 5-currency basket served as the basis for setting the SDR interest rate every calendar quarter. A new uniform basket composed of the U.S. dollar, German mark, French franc, Japanese yen, and pound sterling will be used in the future to calculate both the value of the SDR and the SDR interest rate. By simplifying calculations related to the SDR, this basket should help to facilitate understanding and use of SDR-denominated instruments, both officially and in private markets. The IMF also expanded the uses that can be made of SDR's to cover swap transactions, forward operations, loans, and grants. The list of official institutions other than IMF member countries authorized to accept and hold SDR's was also expanded during the course of the year to include the Swiss

<sup>22</sup> See exhibit 65.



National Bank and a number of international organizations and regional financial institutions.

As additional steps to enhance the role of the SDR, the Secretary of the Treasury proposed at the 1980 IMF/IBRD annual meetings that the interest rate on the SDR be increased from 80 percent to 100 percent of the weighted average of short-term interest rates in the five countries comprising the currency basket; and that the remaining "reconstitution" requirement—which requires that SDR participants hold, on average over a 5-year period, 15 percent of their net cumulative SDR allocations—be eliminated as a means facilitating use of the SDR. Finally the United States suggested that as the private market in SDR's takes hold the World Bank consider borrowing from the private markets in SDR's and lending in SDR terms in order to give further impetus to the asset and to reduce the exchange risks associated with the Bank's operation.

The Secretary also indicated that a properly constructed "international monetary reserve" account could contribute to the longrun stability of the international monetary system. Such an account, by accepting official deposits of dollars and other national currencies in exchange for SDR-denominated claims, would promote the role of the SDR while providing an orderly mechanism for shifts in countries' reserve portfolios. Discussion on the account continued during the year.

During fiscal 1980, the IMF allocated SDR 4,033 million to 139 member countries, including SDR 874 million to the United States. This distribution raised the total amount of allocated SDR's to SDR 17.3 billion. A further allocation of about SDR 4 billion is scheduled for January 1981, and the IMF has begun studying the question of allocations in the next "basic period" beginning in 1982.

#### Participation in the Organization for Economic Cooperation and Development

Assistant Secretary Bergsten attended the meeting of the OECD Council at the Ministerial Level in Paris on June 3-4, 1980. As expressed in the communique issued at the meeting, the Ministers agreed on the appropriate stance of economic policies of OECD member countries in the light of worldwide slow growth, inflationary pressures, and the difficult energy price and supply situation. Ministers also declared their determination to maintain and improve the open and multilateral trading system; gave full support to efforts to bring the credit terms of the Arrangement on Export Credits closer to those of the market; resolved to contribute to the successful outcome of negotiations on a common fund; and affirmed the determination of their governments to contribute adequately to the international aid effort.

OECD bodies which played a key role in reviewing these issues during the year include the Economic Policy Committee (EPC) and its various working parties; the International Energy Agency (see "Commodities and Natural Resources"); and the Trade Committee (see "Trade and Investment").

*Economic policy.*—At their June meeting, OECD Ministers noted that their agreement in 1979 that inflationary pressure from higher oil prices should not be accommodated through monetary or fiscal policy was beginning to have positive results. In most countries, inflation was believed near its peak, while the inevitable loss of real incomes arising from higher oil prices appeared in quite a few countries to be absorbed without significant acceleration of money incomes. Unemployment, however, was seen to be unacceptably high. Ministers agreed that the promotion of conditions for supply-oriented growth involves maintaining a relationship between costs and prices sufficiently favorable to make investment worthwhile, and that, as this and a reduction in inflation are achieved, policies would be followed that ensure that an expanded capital stock would be utilized. It was important as well for positive supply-oriented policies to raise the share of savings and productive investment in GNP and to help improve the operation of product, capital, and labor markets. Ministers agreed that in the shortterm it would be a serious error to relax monetary and fiscal policies until the current surges in inflation have been brought under control; and that once this is achieved, it might be desirable in some countries to resume a less restrictive stance if it is consistent with a balanced medium-term growth path. Ministers agreed that policies to encourage investment in the medium term should include easing the pressure on resources and taxable capacity in countries where public expenditure has been rising too fast; avoiding sharp or unpredictable changes in the direction of policy so as to reduce uncertainty; promoting reforms to remove structural biases against the use of capital and measures to improve the operation of capital markets, increasing the supply of risk capital. Ministers noted the danger that oil price increases in 1979/80 posed for future economic and social development worldwide, and agreed that in the medium term the price mechanism should aid in accelerating the switch from oil to alternative sources of energy.

These economic policy guidelines approved at the OECD Ministerial meeting were largely developed by the OECD's Economic Policy Committee and its working parties on growth and inflation, short-term economic prospects, and external balances. Charles Schultze, Chairman of the U.S. Council of Economic Advisers, continued to serve as chairman of the EPC during this period. The full committee met twice during the fiscal year, in November 1979 and in May 1980.

*Working Party 1 (Macro-economic and Structural Policy Analysis).*—The EPC agreed at its May 20–21 meeting to a proposal merging two working parties that had previously dealt respectively with economic growth and inflation. The merger emphasized the interaction of the two economic phenomena. The new group will focus on medium-term questions, recognizing that medium and longer term growth issues cannot be divorced from stabilization problems and policies.

*Working Party 3 (External Balances).*—During fiscal 1980, the working party was concerned with the interaction between monetary policy and the

adjustment process, the consequences of higher oil prices, and sharply changing balance of payments patterns. Assistant Secretary Bergsten led the U.S. delegation to the March and September 1980 meetings. Deputy Assistant Secretary Widman was the Treasury representative at the December 1979 meeting, and Deputy Assistant Secretary Leddy, the Treasury representative at the May and July 1980 meetings.

*Positive adjustment.*—Work on positive approaches to medium-term structural adjustment continued to be carried out during the year by the special group on Positive Adjustment Policies, attached to the EPC, and by sectoral committees of the OECD such as Industry, Agriculture, and Trade.

#### Economic summits

Treasury officials participated actively in bilateral and multilateral summit activities during the year. Secretary Miller accompanied President Carter and others to the seven-nation economic summit held in Venice June 22–23.<sup>23</sup> Secretary Miller also participated in the U.S./Japan bilateral economic summit in early May.

### Developing Nations

#### Situation of the non-OPEC developing countries

During 1979 and 1980, the aggregate current account deficit of the non-OPEC less developed countries (LDC's) rose sharply, under the influence of large increases in their oil import bills, increases in the costs of nonoil imports, and lower OECD economic growth. In 1979, their combined current account deficit, including official unrequited transfers, reached \$40 billion, \$17 billion above the 1978 deficit of \$23 billion, and over twice the 1977 deficit. In 1980, their combined current account deficit is expected to rise another \$21 billion, to \$61 billion.

About 66 percent of the total deficit in 1979, and 70 percent of the total deficit in 1980, is attributable to a group of 24 important LDC's. For this group, the 2-year cumulative increase in the aggregate petroleum trade deficit amounted to nearly \$11 billion, even though the net volume of oil imported fell in both years. The worsening of their oil deficit was equivalent to 30 percent of the rise in their total deficit in 1979, and 38 percent of the rise in their total deficit in 1980. Another 23 percent of the group's total deficit in 1979, and 34 percent of its total deficit in 1980, can be related to deterioration in the net services balance, in large part resulting from increases in interest payments on accumulated foreign debt.

Other factors tending to increase the non-OPEC LDC deficits were a reduction in the rate of growth of the OECD countries (3.3 percent in 1979 and 1 percent in 1980), and an increase in the overall rate of domestic price inflation in the LDC's (in part, the result of higher oil and nonoil import prices). The GNP-weighted average inflation rate for the 24 LDC's rose from

<sup>23</sup> See exhibit 68.



32 percent in 1978 to 44-45 percent in 1979 and 1980. These factors tended to dampen demand for LDC exports and increase LDC import demand.

During this period of large current account deficits, the overall rate of growth in real GNP for the group of 24 major LDC's was a relatively buoyant 5.2 percent in 1979, and 5.1 percent in 1980, down from 5.9 percent in 1978. However, there was considerable variation in GNP growth rates among the 24 countries, with the oil-exporting countries (Malaysia, Mexico, Peru, Syria, Tunisia, and Egypt) generally achieving higher rates of growth than the oil-importing countries.

Although the non-OPEC LDC's current account deficit was substantial in 1979, financing this deficit appeared to have been relatively easy. With loan demand relatively weak in the developed countries, commercial bank financing was available on exceptionally favorable terms to creditworthy LDC borrowers. Net private financial flows to the non-OPEC LDC's rose to about \$33 billion in 1979, from \$25 billion in 1978. Official financial flows to the non-OPEC LDC's, excluding unrequited official transfers, was \$14 billion in 1979 and a projected \$17 billion in 1980. In 1979, financial flows to the non-OPEC LDC's were so readily available that the non-OPEC LDC's were able to add \$11 billion to their foreign exchange reserves, increasing their reserves (excluding gold assets) to about \$77 billion.

In 1980, the financing situation has shifted dramatically. Medium- and long-term private market lending slowed markedly in the first quarter of 1980 as sharply rising interest rates and financial market uncertainties led both borrowers and lenders to a partial withdrawal from the market. Lending activity picked up later in the year, however. The level of net financing from private sources (especially commercial banks) in the 1980 calendar year may be below the 1979 level. Reflecting the unattractiveness of borrowing on commercial terms, the non-OPEC LDC's as a group are expected to draw down their reserves for the first time since 1975, when the group's current account deficit hit its last cyclical peak.

#### Debt rescheduling

During fiscal 1980, the United States participated in four multilateral debt-rescheduling operations. The debtor countries involved were Sierra Leone, Sudan, Turkey, and Zaire.

The United States and six other official creditors met in Paris on February 7 and 8, 1980, to consider Sierra Leone's request for debt relief. Sierra Leone had been granted debt relief by official creditors once previously in 1977. The current request was viewed favorably by the creditor group because Sierra Leone's debt-servicing problems again had become acute and because the Government had demonstrated clearly its intent to adhere to a stabilization program initiated under an IMF standby agreement implemented in February 1980.

The amounts rescheduled by creditors represented 90 percent of the unpaid portions of certain of Sierra Leone's debt service obligations falling due



during the period from July 1, 1979, to October 31, 1980. Relief was provided also on official external payments arrears outstanding as of July 1, 1979. The amounts related to this period which were rescheduled by participating creditors totaled \$18.4 million. In addition, creditors agreed to extend the rescheduling period to include certain debts falling due between November 1, 1980, and December 31, 1981, contingent on Sierra Leone's obtaining, not later than the end of 1980, access to additional IMF resources under a standby or Extended Fund Facility (EFF). The amounts which would be rescheduled under the latter period total \$11.4 million.

The repayment period for arrears was 7 years without any grace period, and for rescheduled principal and interest relating to the initial 1979-80 period was 12 years including a grace period of 6 years. In addition, creditors agreed in principle to consider a subsequent request by Sierra Leone for rescheduling of 1982 debt service payments, provided that Sierra Leone continues to have an arrangement with the IMF involving use of Fund resources. The United States did not conclude a bilateral agreement with Sierra Leone because the amount of the payments falling due in each of the two consolidation periods was expected to be less than the minimum amount established in the multilateral agreement.

Sixteen of the Sudan's principal creditors, including the United States, met in Paris on November 12 and 13, 1979, and agreed to a rescheduling of part of Sudan's debt service obligations in light of its critical balance of payments situation and its progress to date under an EFF arrangement with the IMF approved in May 1979. At the Paris meeting, the Sudanese authorities made a commitment to seek a rescheduling of Sudanese debts owed to private creditors. Negotiations with private creditors took place in fiscal 1980 but were not concluded.

Official creditors agreed to reorganize 85 percent of the principal and interest falling due during the periods between October 1, 1979, and June 30, 1980, and between July 1, 1980, and June 30, 1981, as well as amounts in arrears as of October 1, 1979. These consolidation periods coincide with the Sudanese fiscal year. Rescheduling of amounts falling due in the latter 1980-81 period was conditioned on Sudan's reaching understandings before June 1, 1980, with the IMF on a second-year program under its current EFF arrangement. The repayment period for rescheduled principal and interest was 10 years, including 3 years of grace, and for payments arrears, 7 years. The rescheduled debt service payments between October 1, 1979, and June 30, 1981, including the arrears that had emerged by October 1, 1979, amount to \$1.38 billion.

The United States subsequently signed a bilateral agreement in Khartoum on May 17, 1980, which implements the terms of the multilateral understanding. Under the terms of the bilateral agreement, payments to be rescheduled by the United States totaled \$11.8 million including both the amounts falling due in the two consolidation periods and amounts in arrears. The weighted average interest rate charged by the United States is 7.94 percent. The U.S.

share of the amounts rescheduled by participating official creditors was less than 2 percent.

For the third consecutive year, Turkey's principal official creditors met in Paris on June 17, 18, and 19, and again on July 22 and 23, 1980, to consider Turkey's request for additional debt relief. The creditors met in the context of a working party of the OECD's Consortium for Turkey. The creditors agreed to an unusually comprehensive multilateral rescheduling agreement. The terms of the rescheduling were justified by the severe economic and financial difficulties facing the country, and by the far-reaching economic recovery program undertaken by a new Turkish Government in January 1980, and supported by an IMF standby arrangement approved in June 1980. The creditors agreed to reorganize 90 percent of debt service payments falling due between July 1, 1980, and June 30, 1981. Conditioned upon Turkey's continued implementation of its 3-year IMF agreement, the creditors also agreed to reschedule on the same terms debt service payments falling due between July 1, 1981, and June 30, 1982, and between July 1, 1982, and June 30, 1983. The repayment period on amounts rescheduled is 10 years, including 5 years of grace. Arrears, as of June 30, 1980, on principal and interest payments relating to both short- and long-term debt were also rescheduled. The repayment period relating to the arrears is also 10 years, including a 5-year grace period. With considerable reluctance, the creditors also agreed to provide debt relief on similar terms for certain arrears for payments under the 1978 and 1979 rescheduling agreements, and for payments falling due between July 1, 1980, and June 30, 1981, under these previous agreements.

[On October 24, 1980, the United States signed a bilateral rescheduling agreement with Turkey to implement the multilateral understanding. Under the terms of the bilateral agreement, payments rescheduled by the United States totaled \$356 million. The weighted average interest rate charged by the United States is 6.7 percent. Under the multilateral agreement, other creditors are expected to provide about an additional \$2.46 billion of debt relief to Turkey.]

A multilateral agreement between Zaire and its principal official creditors was reached during a meeting in Paris on December 10 and 11, 1979. This agreement took into account Zaire's continuing economic and financial difficulties and Zaire's commitment to adhere to a 1-year standby program with the IMF, approved in August 1979.

Creditors agreed to reschedule 90 percent of principal and interest payments falling due between July 1, 1979, and December 31, 1980, with a repayment period of 11 years, including 6 years of grace. Creditors also agreed to reschedule 80 percent of arrears on principal and interest on debt as of December 31, 1979, with a similar repayment period.

The United States subsequently signed a bilateral agreement, in Kinshasa on July 28, 1980, implementing the multilateral agreement. Under the bilateral agreement, payments rescheduled by the United States totaled \$189 million. The weighted average interest rate charged by the United States is 7.74

percent. Under the multilateral agreement, other creditors are expected to provide about an additional \$849.6 million of debt relief to Zaire.

#### Relations with developing nations<sup>24</sup>

*OPEC.*—The combined current account surplus of the 13 members of OPEC is estimated to have increased dramatically for the second year in a row to almost \$110 billion in calendar 1980 from about \$60 billion in 1979. The increase resulted primarily from continued escalations of OPEC oil prices through mid-1980 which followed the Iranian revolution in 1979. These revenue gains more than offset the increased growth of OPEC imports. The surplus continued to be heavily concentrated in five Persian Gulf countries (Saudi Arabia, Kuwait, Iraq, Qatar, and the United Arab Emirates), although there also were significant increases during 1980 in the current account balances of all other OPEC members, except Iran.

OPEC oil earnings (government-take basis) rose from about \$200 billion in calendar 1979 to an estimated \$280 billion in 1980. The Iran/Iraq conflict beginning in late September of 1980 resulted in a near-cessation of their oil exports. Higher oil prices, conservation, and slower economic activity in major oil-consuming countries, and increased non-OPEC production (particularly in Mexico), contributed to a decline in demand for OPEC oil during 1980, following a 3-percent increase during 1979. Reduced demand and record high world oil stocks provided a substantial cushion against upward price pressure at the end of the year. For the year as a whole, production averaged about 12 percent below the 1979 average level.

OPEC oil prices nearly doubled during 1979. In December 1979, OPEC ministers were unable to reach agreement on the level of prices for early 1980. Uncertainties regarding the Iranian situation, the production policies of other OPEC producers, and the Iran/Iraq conflict contributed to OPEC oil price increases averaging an additional 25 percent during 1980 to over \$33/bbl, including premiums. At the OPEC ministerial meeting in June 1980, a maximum price for OPEC oil was set at \$37 per barrel, a guideline followed by most producers for official prices, but often exceeded taking price premiums into account.

It is estimated that the aggregate value of OPEC imports grew by about 25 percent in 1980, to about \$140 billion. The growth rate was faster than the 4-percent increase during 1979, which reflected a sharp drop in Iranian imports and stagnation of Algerian, Nigerian, and Venezuelan imports. In 1980, strong import growth occurred in all OPEC countries. The volume of aggregate OPEC imports is estimated to have increased by 10 to 15 percent in 1980, as compared with a decline of 5 to 10 percent in 1979.

*Middle East/Turkey.*—Following the seizure of the American hostages and threats by the Government of Iran that it would not honor its financial obligations to U.S. citizens and entities, the U.S. Government responded with

<sup>24</sup> See exhibits 74 and 80.



a series of actions including the blocking of Iranian assets on November 14, 1979.<sup>25</sup>

Secretary Miller visited the Middle East in November 1979 to discuss a broad array of economic and financial issues with officials of Saudi Arabia, the United Arab Emirates, and Kuwait. The trip represented a continuation of the administration's dialog with these important countries. The Secretary met again with officials from Saudi Arabia and Kuwait during the annual meetings of the IMF/IBRD in September 1980 and discussed, among other things, energy and financial matters.

Secretary Miller and former Under Secretary for Monetary Affairs Solomon met on several occasions during the year with representatives of the Government of Turkey to discuss issues of mutual concern, including debt relief. Also, the U.S. Government was a major donor to the special economic assistance package assembled for Turkey in April 1980 and provided under the auspices of the OECD.

Assistant Secretary Bergsten met with officials of the Government of Israel several times in 1980, and he cochaired the semiannual meeting of the Bi-National Research and Development Foundation which met in Washington in early June.

*Asia.*—Busy schedules militated against policy-level Treasury officials' visits to the Asian LDC's this year. Nevertheless, numerous high-level meetings took place with Asian officials in Washington. Secretary Miller met with Korean Deputy Prime Minister Lee Hahn Been on February 20, 1980, to discuss Korea's political and economic situations. On April 17, Secretary Miller met with the Philippines Minister of Finance Cesar Virata. Minister Virata also served as Chairman of the IMF/IBRD Development Committee. Bilateral trade and investment issues as well as multilateral development and finance issues relating to the international financial institutions were discussed by the participants. Secretary Miller and Minister Virata met again on September 10. Once again a broad range of issues was discussed, including trade finance. Secretary Miller addressed a luncheon of the Association of Southeast Asian Nations (ASEAN) Section of the U.S.-ASEAN Business Council on May 29.

During the annual meetings of the IMF/IBRD, the Secretary held meetings with Korean Minister of Finance Lee Seung Yun and Indonesian Minister of Finance Ali Wardhana.

Assistant Secretary Bergsten met twice during the year with Malaysian Minister of Primary Industries Paul Leong. Discussions focused on commodity issues, including the Common Fund. The meetings took place in Washington on February 5 and September 2. The Assistant Secretary also met with Chung Hoon Mok, Special Assistant for Economic Affairs to Korean Prime Minister Nam Duck Woo, on September 5. Their meeting focused on issues relating to the annual meetings of the IMF/IBRD. During

<sup>25</sup> See section concerning Iran under the administrative report of the Office of Foreign Assets Control and exhibits 40 and 72.



the IMF/IBRD meetings, Assistant Secretary Bergsten met with Sir Philip Haddon-Cave, Financial Secretary of Hong Kong. During these meetings Deputy Assistant Secretary Nachmanoff met with Oudone Pholsena, Deputy Governor of the Lao National Bank. Deputy Assistant Secretaries Nachmanoff, Schotta, and Hufbauer participated in a panel discussion with the ASEAN Section of the U.S./ASEAN Business Council on May 29.

*Latin America.*—During the year, Secretary Miller and Assistant Secretary Bergsten met with Mexican Finance Minister David Ibarra Munoz and Bank of Mexico Chairman Gustavo Romero Kolbeck on a number of different occasions to discuss United States-Mexican economic relations, the world economic outlook, tax and trade matters, and access to capital markets, as well as measures to help deal with developing country economic problems.

In April 1980 Deputy Secretary Carswell headed the U.S. delegation to the annual meeting of the Inter-American Development Bank in Rio de Janeiro, Brazil.<sup>26</sup> At that time Deputy Secretary Carswell and Deputy Assistant Secretary Nachmanoff held a number of bilateral meetings with the heads of Latin American delegations to discuss economic relations with the individual countries, regional economic problems, and the world economic outlook and recycling problems and prospects.

Secretary Miller and Assistant Secretary Bergsten in October 1979 met with Brazil's Finance Minister at the time, Karlos Rischbieter, and the then President of the Central Bank, Ernane Galveas, to discuss U.S.-Brazil relations, the economic outlook, and topics of mutual interest during the annual meetings of the IMF/IBRD. This was followed in February 1980 by a meeting between Antonio Delfim Netto, Brazil's Planning Minister, Minister of Finance Galveas, and Secretary Miller, Under Secretary Solomon, and Assistant Secretary Bergsten. Deputy Secretary Carswell met with Finance Minister Galveas and Central Bank President Carlos Langoni in April to discuss the world energy outlook, capital markets, and a variety of bilateral issues. As the fiscal year drew to a close, preparations were underway for meetings between Secretary Miller and Brazilian officials at the annual IMF/IBRD meetings in the first week in October.

Secretary Miller and Assistant Secretary Bergsten met in March with Venezuelan Energy Minister Calderon Berti and Venezuelan Ambassador Perez Chiriboga to discuss the world oil market, hemispheric energy cooperation, and aid for Western Hemisphere countries.

Deputy Secretary Carswell met with Argentine Minister of Economy Martinez de Hoz in April. This was followed by a meeting between the Minister and Secretary Miller a month later to discuss a number of bilateral issues and changing world economic conditions. In June, Secretary Miller met with Argentine Secretary of Planning and Economic Coordination Guillermo Walter Klein, Jr.

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<sup>26</sup> See exhibit 76.

Secretary Miller met with Peruvian Government officials in Washington in February and October. The October meeting, with key members of the new, democratically elected Belaunde administration, included discussion of Peru's economic progress, trade policies, and U.S. economic assistance.

*Africa.*—Treasury officials continued to maintain an active role in U.S. economic relations with Africa during the year. Secretary Miller, Deputy Secretary Carswell, Assistant Secretary Bergsten, and Deputy Assistant Secretary Nachmanoff met with officials from Zaire, Liberia, Senegal, and Zambia on several occasions to review their efforts to stabilize their economies. Secretary Miller also met with Tanzania's finance minister, in the minister's role as chairman of the IMF/IBRD annual meetings. Deputy Secretary Carswell met with Tunisia's Minister of Finance Mansour Moalla during the annual meetings of the IMF/IBRD. They discussed Tunisia's development plan and economic needs. Assistant Secretary Godley led the U.S. delegation to the annual meeting of the African Development Fund in Abidjan from June 23 to 25.

#### Development Committee

North-South issues have claimed increasing prominence in the last year as the global economic situation has become increasingly severe, especially for the oil-importing developing nations.<sup>27</sup> The United Nations, and its specialized fora, provide important mechanisms for exploring development issues and for progress in the North-South dialog. The IMF/IBRD Development Committee, on which the United States is represented by the Secretary of the Treasury, considers a broad range of international economic issues within the purview of the IBRD and IMF.

The Development Committee was established in 1974 by the Governor of the World Bank and the International Monetary Fund and is composed of 20 members, equally divided between developed and developing nations. The Committee maintains an overview of the development process, considers all aspects of the question of the transfer of real resources to the developing countries, and makes suggestions for consideration for the implementation of its conclusions.

The focus of the two Development Committee meetings held in 1980 was on the changing global economic relationships and the bleak medium-term prospects for the world economic growth. Higher real costs of energy, expected slow growth in the industrialized countries, and persistent high rates of inflation were pointed out as factors contributing to serious and prolonged payments imbalances expected for certain oil-importing countries.

The Committee urged that developing countries undertake economic policies designed to adjust to present economic circumstances and that industrialized countries pursue policies that would not hinder this process.

<sup>27</sup> See exhibits 73 and 80.

Financing developing country requirements through private foreign investment, nonconcessional flows, and concessional flows was discussed.

The Task Force on Private Foreign Investment, chaired by Assistant Secretary Bergsten, recommended that the World Bank undertake a study of investment incentives and performance requirements. In its final report, the task force (1) endorsed the objectives of seeking an international understanding which would limit the adverse effects of incentives and of considering what further actions might need to be taken concerning performance requirements, and (2) recommended that the World Bank group study countries' use of such measures and possibly consider developing a concept and terms upon which an international understanding in this area might evolve. The Committee noted that further analysis of private foreign investment might lead to a better understanding of important factors in both investor and host countries that determine the volume and nature of such investments and suggested that the Bank consider undertaking such a study.

In February 1980 the Development Committee, in response to discussions at its September 1979 meeting in Belgrade, established a Task Force on Non-concessional Flows to examine proposals to increase nonconcessional financial flows to LDC's, to assess conditions in international capital markets that bear on this goal, and to consider the role of export credit institutions in facilitating nonconcessional flows. The task force is examining the capability of the international financial system to facilitate recycling of surpluses, as in the 1974-76 period, so that countries can obtain financing, to ease the pain of adjustment to increased oil costs.

The group held four meetings in the last half of fiscal 1980 and presented a progress report to the Development Committee at the IMF/IBRD annual meetings in September 1980. Reference in the progress report to ways in which the IMF and the multilateral development banks increased their lending capacities and examination of further possibilities reflects an emerging consensus, promoted and strongly endorsed by the United States, to emphasize the existing (and recently improved) institutional framework of the Bank and Fund. With its statement that "developing countries could continue to improve their creditworthiness by adopting economic policies, including adjustment programs where necessary," the progress report recognizes an essential complement to increased nonconcessional flows to LDC's.

The task force requested the World Bank to prepare a full study of a number of proposals (including several which have been suggested and reviewed in the past) for some possible courses of action which may be given more serious consideration depending upon future needs. At the suggestion of the United States, the Bank is to analyze these proposals against a framework of key criteria, e.g., additionality, creditworthiness, and portfolio concentration. This should facilitate an objective review of the proposals' strengths and weaknesses. The Committee endorsed the task force's request to the World Bank for a full study of the various proposals under its consideration.



It is agreed that least-developed and low-income countries deserve special attention in view of their large financing needs and longer term adjustment investment requirements. In view of the unfavorable outlook for concessional assistance, the Committee requested that the IBRD undertake a study on possible ways to increase volume and quality of concessionary assistance.

The Committee welcomed Bank and Fund consideration of the recommendations of the Brandt Commission, the Group of 24 "Program of Immediate Action," and the Bank's initiative to examine the possibility of establishing an energy affiliate to promote expansion of its lending operations in the energy sector. The Committee noted the recent increase in demand for the Bank's financial assistance to support structural adjustment programs, energy lending, and China's development efforts. These factors, coupled with the fact that previous planning assumptions had been based on lower rates of world inflation than those now prevailing, led the Committee to urge the Board of the World Bank to explore appropriate ways to expand the lending capacity of the Bank above present and projected levels.

#### Local currency management

One of the responsibilities of the Secretary of the Treasury is to determine which foreign currencies held by the United States are in excess of normal U.S. Government requirements. The purpose of this determination is to assure maximum use of local currencies in lieu of dollars for U.S. programs in the countries concerned. For fiscal 1981, Burma, Egypt, Guinea, India, and Pakistan are on the excess currency list.

As U.S. foreign currency receipts decrease and in-country expenses increase, currencies lose their excess status. When countries are removed from the excess list, special foreign currency programs in those countries are phased out. These programs include scientific and research projects which usually have some political benefit to the United States but, because of their lower priority, might not be funded were it not for the availability of excess currencies.

#### Development assistance policy

The Department of the Treasury, in addition to its responsibilities with regard to the multilateral development banks, participates in the formulation of U.S. development assistance policy through its membership in the National Advisory Council on International Monetary and Financial Policies, in the Development Coordination Committee (DCC), and in various other interagency committees designed to coordinate economic assistance programs. Treasury's principal concerns are to promote the efficient utilization of development assistance resources and to assure that bilateral aid objectives and programs remain consistent with overall U.S. economic interests and with U.S. multilateral aid efforts, in particular.

As a member of the DCC, Treasury has actively supported measures to strengthen that Committee's policy coordinating role. Treasury participates



in each of four subcommittees which treat issues in the specific areas of multilateral assistance, bilateral assistance, food aid, and international organizations. As a reflection of its special responsibilities for U.S. policy toward the multilateral development banks, a senior Treasury official has served as chairman of the DCC Subcommittee on Multilateral Assistance, which this year considered the World Bank's proposal on structural adjustment lending; cofinancing between U.S. private lenders and the multilateral banks; new aid donor performance measures; Brandt Commission proposals relating to the World Bank; procurement by international organizations; and replenishment of the resources of the International Fund for Agricultural Development. The Subcommittee's Working Group on Multilateral Assistance continued its ongoing review of development projects proposed by the banks.

In addition to the work of its Subcommittees, the DCC undertook several country strategy reviews focusing on development problems of selected high-priority countries. The purpose of these reviews is to formulate a coherent U.S. development assistance strategy toward individual countries, integrating a full range of programs and policies. During the year, the DCC conducted strategy reviews on Indonesia, the Philippines, and Kenya.

Another highlight of DCC work this year was its review of the balance between U.S. bilateral and multilateral assistance and the allocation of new funds between these channels. In this review, the DCC examined issues concerning resource control, policy leverage, efficiency, and U.S. domestic considerations.

Parallel to Treasury's active participation in the ongoing work of the DCC, it was also directly involved in interagency consultations with the International Development Cooperation Agency (IDCA). This year Treasury has worked closely with IDCA in facilitating coordination between bilateral and multilateral assistance programs, in formulating U.S. Government budgetary strategy for providing assistance to the Third World, and in developing a program to increase the use of capital saving technology in development assistance.

#### Multilateral development banks<sup>28</sup>

During fiscal 1980, the administration requested appropriation of funds for U.S. participation in the multilateral development banks for fiscal 1981. A breakdown of the request is shown in the table below. At the end of fiscal 1980, final congressional action on the request was pending.

At the end of fiscal 1979, legislation was also pending in Congress to authorize U.S. participation in replenishment of resources for the International Development Association (\$3.240 billion over a 3-year period beginning in fiscal 1981) and U.S. membership in the African Development Bank (\$360 million over a 5-year period beginning in fiscal 1981).

<sup>28</sup> See exhibits 75, 77, 78, and 80.

*Appropriation request for U.S. participation in the multilateral  
development banks during fiscal 1981*  
[\$ millions]

Institution	Fiscal 1981 appropriation request	Comment
International Bank for Reconstruction and Development:		
Paid-in .....	86.3	Third and remainder of second installments of U.S. subscription to IBRD selective capital increase authorized in fiscal 1977.
Program limitation on callable subscription .....	776.5	
International Development Association .....	1,100.0	\$1,080 million represents the first installment of the U.S. contribution to the sixth replenishment of IDA. \$20 million represents the remaining portion of the U.S. contribution to IDA's fourth replenishment.
International Finance Corporation .....	14.4	Remainder of third installment of U.S. contribution to IFC authorized in fiscal 1977.
Inter-American Development Bank:		
Paid-in .....	58.9	Second and remainder of first installments of U.S. subscription to fifth IDB replenishments.
Program limitation on callable subscription .....	727.0	
Fund for Special Operations .....	325.3	\$150.3 million remains to be appropriated from replenishment authorized in fiscal 1976.
Asian Development Bank:		
Paid-in .....	29.8	Third and final installment of U.S. subscription to second ADB capital increase authorized in fiscal 1977. \$85 million callable and \$9.4 million paid-in remains to be appropriated for the second installment.
Program limitation on callable subscription .....	268.2	
Asian Development Fund .....	171.3	The second installment of U.S. contribution to the third replenishment and a portion of U.S. contribution to the second ADF replenishment.
African Development Bank:		
Paid-in .....	18.0	First of five annual installments of initial U.S. subscription to AFDB.
Program limitation on callable subscription .....	53.9	
African Development Fund .....	58.3	Second and remainder of first installments of U.S. contributions to the second AFDF replenishment.
Total budget authority .....	<u>1,862.3</u>	
Total program limitations on callable capital .....	1,825.7	

The multilateral development banks committed \$16,418 million to developing countries in fiscal 1980. The distribution of these commitments by institution was as follows: World Bank group, \$12,569 million; Inter-American Development Bank, \$2,168 million; Asian Development Bank, \$1,433 million; and the African Development Fund, \$247.7 million.

Participation in the multilateral development banks is an efficient and cost-effective way for the United States to help promote economic growth and social development in less developed countries. All lending operations are based on sound financial and operational criteria; each proposal must pass through a detailed and rigorous appraisal process, thus assuring that the greatest developmental impact is obtained from every dollar lent.

The United States shares the burden for providing economic assistance with other donor countries. These countries provide \$3 for every dollar contributed by the United States. In addition, 70 percent of the banks' total lending requirements are met by borrowings from private capital markets. These borrowings are backed by callable capital subscriptions which do not result in actual budgetary outlays by the United States or other donor countries. In the case of the World Bank, each dollar paid in by the United States has led to \$50 of Bank lending.

There are also substantial financial and economic benefits which accrue directly to the United States as a result of participation in the multilateral development banks. In the case of the World Bank, the United States pays in less than 2 cents for each dollar loaned out by the Bank and gains 18 cents in procurement contracts awarded to U.S. firms, thus increasing income and employment levels in the domestic economy. There are also significant indirect benefits to the U.S. economy as a result of the increased growth of less developed countries which is fostered by development bank lending activity.

The multilateral development banks also have been extremely responsive to U.S. policy initiatives that a greater effort be made to help meet basic human needs in recipient countries and to ensure the participation of the poor in the benefits of development. The World Bank has also initiated a structural adjustment lending program which is designed to assist borrowing countries make those changes in economic policy which are required as a result of higher energy costs. In the field of energy, the banks have also acted to meet basic U.S. policy concerns and placed greatly increased emphasis on lending programs to expand and diversify alternative sources of energy in non-OPEC developing countries. Over the next 5 years, World Bank lending for energy development is projected to reach about \$13 billion, and to support projects totaling \$56 billion. This volume of lending is expected to result in the production of energy equivalent to 2.5 million barrels of oil a day. When hydroelectric power projects are included, about 20 percent of overall Bank lending during the next 5 years will be for energy purposes.

Over the next several years, the Inter-American Development Bank will be devoting a greater proportion of its lending to help develop geothermal and hydroelectric potential in Latin America, and the Asian Development Bank has embarked on a large lending program to finance the production of primary energy fuels. These bank funds will also have the effect of facilitating additional private investment in this critical area, thus improving the oil supply and demand balance for the world as a whole.



### World Bank group

The World Bank group (IBRD, IDA, IFC) committed a total of \$12,569 million for economic assistance to its borrowing member countries in fiscal 1980, an increase of 24 percent over the previous fiscal year. Lending extended on nonconcessional terms from the IBRD amounted to \$8,164 million in fiscal 1980, compared with \$7,182 million in fiscal 1979, an increase of almost 14 percent. New IDA credits, which are highly concessional, reached \$3,724 million in fiscal 1980, up \$1,127 million from the \$2,597 million level of the previous fiscal year. IFC commitments were \$681 million in fiscal 1980, compared with \$354 million in fiscal 1979. As of September 30, 1980, total IBRD loan commitments outstanding were \$520 billion. The comparable figure for IDA credits was \$20.9 billion. Cumulative gross commitments by the IFC totaled \$3.2 billion as of that date.

During fiscal 1980, the IBRD and IDA continued to emphasize lending for agriculture and rural development. IBRD loan commitments in this sector in fiscal 1980 were \$1,992 million (24 percent of total lending) and IDA commitments were \$1,510 million. The amounts committed by IDA for agricultural purposes continued to be the highest (41 percent of total lending in fiscal 1980) of any sector. Other important sectors in IBRD and IDA lending programs for fiscal 1980 included development finance, industry, power, transportation, and water supply and sewerage. The IBRD's lending for oil, gas, and coal production rose fourfold (to slightly over 4 percent of new commitments) in fiscal 1980, and is expected to increase still further in the future. The IBRD also began a program of medium-term structural adjustment lending to assist LDC's adjust to higher energy prices and other adverse global economic trends, while simultaneously maintaining their development programs. Structural adjustment lending will be conditioned upon specific micro and macroeconomic policies aimed at improving the borrowing country's fundamental balance of payments position.

The World Bank group provided resources in fiscal 1980 to 77 countries distributed geographically as follows: Sub-Saharan Africa, 30 countries (\$1,608.9 million); Asia and Pacific, 15 countries (\$4,969.4 million); Latin America and Caribbean, 18 countries (\$3,540.7 million); and Europe, Middle East, and North Africa, 14 countries (\$2,449.6 million).

In his address at the 35th joint annual meeting of the International Monetary Fund and the World Bank in Washington, D.C.,<sup>29</sup> shortly after the end of fiscal 1980, Secretary of the Treasury (and U.S. Governor) Miller highlighted the challenges facing World Bank developments efforts, and emphasized the vital importance of the Bank's remaining at the forefront of global efforts to deal imaginatively with the changed world economic situation. Secretary Miller (1) attached great importance to the Bank's plan for energy development in oil-importing developing countries, and expressed strong support for the Bank's search for ways to expand energy development

<sup>29</sup> See exhibit 71.



efforts; (2) applauded the Bank's efforts to assist developing countries to strengthen their future growth and development through its new program of medium-term loans for "structural adjustment"; (3) praised the Bank's efforts in the population area and urged increased lending in this sector; and (4) urged that the Bank's solid achievement in maximizing project benefits for the poor be maintained, and the share of lending allocated to the poorer borrowing countries be increased. Secretary Miller also called for innovation in collaboration between the IBRD and IMF to help member countries in assessing their economic prospects, developing effective economic programs, and providing appropriate financing. He also noted the essential need for the Bank and Fund to remain as autonomous institutions with distinct functions and purposes. Secretary Miller expressed full support for the Bank's general capital increase and the sixth replenishment of IDA.

Lending operations of the IBRD are financed from the following sources: The convertible currency portion of paid-in capital subscriptions from member countries; borrowings in private capital markets and from governments and central banks; sales of loan participations; principal repayments on previous loans; and retained earnings on loans and investments.

During the Bank's most recent fiscal year (July 1, 1979, to June 30, 1980), its outstanding debt obligations increased \$3,388 million to \$29,668 million. As of June 30, 1980, estimates of the outstanding borrowings by principal source were:

Country	Principal amount (US\$ millions)	Percentage of total outstanding amount
Germany .....	8,223	27.7
United States .....	5,844	19.7
Switzerland .....	4,730	15.9
Japan .....	4,173	14.1
OPEC .....	4,206	14.2
Other .....	2,492	8.4
Total .....	29,668	100.0

The "other" category of 8.4 percent of outstanding borrowings was held by central banks, government agencies, and investors in more than 70 countries.

Total borrowings by the IBRD in World Bank fiscal 1980 amounted to the equivalent of \$5,173.4 million. The IBRD sells its securities through placement directly with governments, government agencies, and central banks, and in the public markets where securities are offered to investors through investment banking firms, merchant banks, or commercial banks. Of the 42 borrowing operations that the IBRD conducted during World Bank fiscal 1980, 31 were public issues or private placements. These issues accounted for \$3,503.9 million, or 68 percent of total funds borrowed. The other 11 issues, totaling \$1,652.9 million, or 32 percent of the funds raised, were placed with official sources (member governments of the World Bank, central banks, and government institutions). The main sources for the IBRD's public and private borrowings in World Bank fiscal 1980 were Germany (\$2,045.2 million), Japan (\$742.2 million), and Switzerland (\$669.6 million). The IBRD also borrowed

\$500 million in the Eurobond market. The IBRD did not borrow in the U.S. market during this period.

Net income of the IBRD in World Bank fiscal 1980 was \$587.9 million, an increase of \$181.4 million (nearly 45 percent) over the World Bank fiscal 1979 level. Income on IBRD investments was \$834.5 million in World Bank fiscal 1980, up \$90.6 million, or almost 12.2 percent, from the World Bank fiscal 1979 level of \$743.9 million. Income on loans and from commitment fees rose by \$275.9 million, or 16.5 percent, to reach \$1,944.7 million. During this same period, sales of participations in the IBRD's loan portfolio amounted to \$23 million, as compared with loan sales of \$66.8 million in World Bank fiscal 1979. Following a practice established in previous years, the IBRD again transferred a portion of its net income to the IDA as a grant. This transfer was \$100 million in World Bank fiscal 1980, the same level as in previous fiscal years.

The IBRD's income statement comparing the World Bank fiscal years ended June 30, 1980 and 1979, is shown below:

<i>Expressed in United States dollars (in thousands)</i>		
	July 1-June 30	
	1979/80	1978/79
<b>Income:</b>		
Income from loans:		
Interest .....	1,800,996	1,543,471
Commitment charges .....	143,787	125,371
Income from investments .....	834,498	743,940
Other income .....	20,249	11,788
<b>Total income .....</b>	<b>2,799,530</b>	<b>2,424,570</b>
<b>Expenses:</b>		
Interest on borrowings .....	1,975,469	1,817,395
Administrative expenses .....	197,967	172,027
Bond issuance and other financial expenses .....	38,193	28,606
<b>Total expenses .....</b>	<b>2,211,629</b>	<b>2,018,028</b>
<b>Net income .....</b>	<b>587,901</b>	<b>406,542</b>

In March 1980, after a series of meetings involving representatives of prospective donor governments to a sixth replenishment of IDA, the Governors of the Association approved a resolution enabling a \$12 billion replenishment for the 3-year period beginning in July 1980. However, at the end of the U.S. fiscal year this replenishment was still not effective, as necessary formal notifications of donor intention to make payment or seek appropriation of commitments totaling about 80 percent of the total sixth replenishment had not been received. A number of countries agreed—as an interim measure pending implementation of the sixth replenishment—to make advance individual contributions beginning in October 1980.

Legislation for U.S. participation in IDA VI was pending at the time this report was under preparation. The U.S. share of the replenishment is 27 percent, and therefore it is impossible for the replenishment to come into

effect without U.S. participation. (The U.S. share in IDA V was 31.04 percent.) The United States will be able to agree to participation in the replenishment only after obtaining authorizing legislation for its \$3.24 billion share and appropriation for its first payment.

#### Inter-American Development Bank

During fiscal 1980, the Inter-American Development Bank (IDB) committed a total of \$2,168 million, a 7-percent increase in lending over fiscal 1979. Of this amount, \$1,279 million was lent on conventional terms from the capital account; \$799 million was lent on concessional terms from the Fund for Special Operations (FSO). In addition, the Bank committed \$90 million in funds administered for various donors (primarily the Venezuelan trust fund). As of September 30, 1980, cumulative lending by the Bank was \$16.7 billion, of which \$8.7 billion had been lent from capital, \$6.8 billion from the FSO, and \$1.1 billion from other resources, primarily the U.S. social progress trust fund and the Venezuelan trust fund.

In terms of sectoral concentration, energy and agriculture received the greatest amount of Bank financing during fiscal 1980. Other sectors receiving substantial amounts of Bank funding included industry, transportation and communications, environmental and public health, education, export financing, preinvestment, and tourism.

IDB lending operations are financed for the most part from borrowings in international capital markets, based on callable capital subscriptions of member countries, as well as from paid-in capital subscriptions and contributions to the FSO. The total subscribed capital of the Bank as of September 30, 1980, was \$13,230 million, of which \$1,521 million was paid-in and \$11,709 million was callable. The resources of the FSO as of the same date amounted to \$7,663 million. The U.S. subscriptions to IDB capital totaled \$4,647 million, or approximately 35 percent. Including contributions which were fully authorized, but not completely appropriated, U.S. contributions to the FSO amounted to \$4,270 million, or 56 percent of the total resources contributed for concessional purposes.

In fiscal 1980, the Inter-American Development Bank borrowed a total of \$491.6 million or its equivalent from the international capital markets. This total included \$100 million from U.S. capital markets with the remainder coming from capital markets of Western Europe and Japan, including \$49.7 million of short-term bonds sold to central banks in Latin America and the Caribbean and \$37.5 million of short-term to central banks in nonregional countries. As of September 30, 1980, the Bank's outstanding funded debt amounted to \$3,151 million.

As discussed in last year's Annual Report, a major replenishment of the Bank's resources totaling \$9.75 billion (\$8 billion for capital stock, \$1.75 billion for the FSO) for the 1979-82 period was agreed to by the United States and other member countries during fiscal 1979. The replenishment did not enter into effect, however, until July 1980 when the United States,



following passage of authorizing legislation by Congress, was able to vote in favor of the resolutions to increase the Bank's capital stock and the resources of the Fund for Special Operations. At that time, in partial fulfillment of the first installment of the replenishment, the United States subscribed \$44.2 million to paid-in capital and \$544.5 million to callable capital, and contributed \$175 million to the FSO.

At the 1980 annual meeting of the IDB in Rio de Janeiro, Brazil,<sup>30</sup> Deputy Secretary Carswell, as Acting U.S. Governor, noted the Bank's pioneering work in the fields of land reform, integrated rural development, public health, and urban development. He also commended the Bank for devoting an increasing share of its lending to the energy sector. Deputy Secretary Carswell encouraged the IDB to devote more attention to the two problem areas of inadequate food supply and rapid population growth.

#### Asian Development Bank

Asian Development Bank (ADB) lending in fiscal 1980 reached \$1,433 million, as compared with \$985 million for fiscal 1979; loans from Ordinary Capital resources totaled \$979 million, as compared with \$563 million in fiscal 1979; loans from Special Funds amounted to \$454 million, as compared with \$402 million in 1979. Cumulative ADB lending as of September 30, 1980, amounted to \$6,696 million, of which \$4,719 million was from Ordinary Capital resources and \$1,977 million was from Special Funds resources. Agriculture and agro-industry accounted for the largest share of Bank lending followed by energy and social infrastructure projects. The largest borrowers from ADB's Ordinary Capital resources in fiscal 1979 were Indonesia, the Philippines, and Korea. The largest borrowers from Special Fund resources were Pakistan and Bangladesh.

ADB Ordinary Capital lending operations are financed with resources borrowed from governments, central banks and private capital markets, paid-in capital subscriptions, repayments of principal and interest on loans, and net earnings on investment. Asian Development Fund resources used for concessional loans are contributed by member countries. During fiscal 1980, the United States subscribed to \$155 million Ordinary Capital shares, raising total U.S. subscriptions to \$1,209 million (out of a total subscribed capital of \$9,000 million), giving the United States an 11-percent voting share. The United States also contributed \$111.25 million to the resources of the Asian Development Fund, (ADF), raising our total contribution to the ADF to \$381 million (out of a total contribution of \$2,625 million from all sources). During fiscal 1980, gross borrowings by the ADB were \$356 million; total outstanding borrowings of the Bank at the end of the fiscal year were \$1,892 million.

At the 13th annual meeting of the ADB Board of Governors in April 1980, Deane R. Hinton, Assistant Secretary of State for Economic and Business

<sup>30</sup> See exhibit 76.



Affairs, and Acting U.S. Governor, reaffirmed our commitment to the ADB and to the Asian and Pacific region. He commended the ADB for its success in satisfying many of the basic needs and aspirations of the Bank's developing member countries. During fiscal 1980, the Bank entered several new areas of activities: It made its first program loan for industry, the first loan for rural electrification, the first multiproject loan—a loan package designed to assist small island economies—and a new integrated type of program loans for crop intensification. In addition, the replenishment of the Asian Development Fund (ADF III), designed to cover the Bank's concessional lending needs over the 4-year period from 1979 to 1982, came into effect during the year.

#### African Development Fund

The African Development Fund (AFDF) was created on July 3, 1973, as the concessional lending affiliate of the African Development Bank (AFDB). The AFDF is designed to channel resources to the poorest African nations; except in the most unusual circumstances, its loans are not extended to countries with a per capita GNP in excess of \$550.

The United States joined the AFDF in November 1976 with an initial contribution of \$15 million and has contributed an additional \$60 million since 1977. In addition to the United States, membership in the AFDF includes 13 European countries, Argentina, Brazil, Canada, Japan, Korea, Kuwait, Saudi Arabia, the United Arab Emirates, and the AFDB. Total resources pledged to the fund amounted to \$1,365 million as of September 30, 1980.

In fiscal 1980 AFDF lending amounted to \$247.7 million, distributed among 23 African countries. This represented an increase of \$40.1 million, or 19 percent, above the 1979 lending level of \$207.6 million. Among the largest borrowers in 1980 were Ethiopia, Burundi, Gambia, and Zambia.

AFDF lending in 1980 was used to finance projects in the agricultural, transportation, health, and education sectors. Agriculture accounted for the largest proportion of lending, ranging from rural development and extension of farming techniques to development of irrigated farming, rehabilitation of plantations, and infrastructural works. It is expected that this particular pattern of lending will continue inasmuch as the possibilities for improving the living conditions in recipient countries depend importantly on agricultural development. Transportation and education and health represented the sectors receiving the second and third highest amounts of lending, respectively.

The seventh annual meeting of the African Development Fund was held in Abidjan, Ivory Coast, in June 1980. The U.S. representative at this meeting reviewed some of the prospects for the world economy in the eighties, emphasizing the negative impact the new surge in energy prices will have on growth and inflation rates in both developed and developing countries. He stressed the importance of a healthy U.S. economy and dollar to developing nations and outlined some of the belt-tightening measures the administration had taken to put our economy on a stable growth path. He reaffirmed the

U.S. commitment to African development, expressed U.S. support for the African Development Bank and Fund, and reviewed U.S. policies to assist Africa. He also expressed satisfaction with the African Development Fund's lending priorities, especially the increasing emphasis on the agricultural sector, and applauded the measures adopted by management to improve internal administration.

### International Economic Analysis<sup>31</sup>

#### Office of Trade Research

The Office of Trade Research is responsible for analyzing international trade and commercial policy issues. During fiscal 1980, the Office of Trade Research undertook and completed a number of research projects and activities. Among the major projects completed are the following:

*The role of State development agencies in U.S. positive adjustment.*—This study described State incentive programs and analyzed whether they encourage transfer of resources out of declining industries and into ones in which demand is growing, and from less to more efficient production, i.e., promote "positive" adjustment. An empirical analysis found the pattern of State aid to investment to be strongly consistent with the pattern of U.S. specialization in international trade and, hence, to support positive adjustment.

*The industry-country incidence of "less than fair value" cases in U.S. import trade.*—This project investigated aspects of two important avenues of administered protection in the United States, the antidumping and countervailing duty mechanisms. These mechanisms are intended to control sales of products in the U.S. market at less than their "fair value" by virtue of a foreign export subsidy. The study tabulated and analyzed the dispersion of less-than-fair-value (LFV) complaints and LFV affirmative findings across both industry categories and countries that exported to the United States between 1975 and 1979. An exploratory empirical analysis was also undertaken using cross-sectional regression methods. The results indicate that LFV complaints have a negative impact on import growth.

*The political economy of administered protection.*—This study sought to identify the determinants of findings brought under the major U.S. instruments for administered regulation of imports—enforcement of the antidumping and countervailing duty laws and the operation of the escape clause mechanism. A theory of how these mechanisms work distinguishes political from technical factors influencing decisions. Various implications of this theory were tested empirically against the record of countervailing duty, antidumping, and escape clause cases over 1975–79. The analysis found that LFV injury decisions are predominantly shaped by political factors, while LFV pricing decisions are mainly determined by technical factors related to

<sup>31</sup> See exhibit 79.

U.S. comparative advantage. Because of the small number of escape clause decisions, the empirical analysis of these decisions was not definitive.

*Import competition and price-setting behavior of U.S. manufacturers.*—The proposition that imports discipline the ability of domestic producers to raise prices above the competitive and socially efficient level of their actual production costs has long been a part of the case for a liberal trade policy. This study investigated that proposition empirically using a pooled cross-section of data on U.S. manufacturing industries and on U.S. imports, taking into account the two-way relationship between domestic price changes and import penetration. It found that import penetration of U.S. markets does have a significant negative effect on U.S. domestic manufacturing prices, and that this effect is larger the more highly concentrated in the U.S. industry.

The Office also completed a number of lesser projects, including assessing the competitive positions of U.S. industries, examining the macroeconomic factors affecting U.S. trade performance, and investigating whether U.S. manufacturing prices are more responsive to increases than to decreases of production costs (ratchet phenomena).

#### U.S. balance of payments developments

The Office of Balance of Payments has staff responsibility for briefing and advising the Secretary and other officials on recent and prospective developments in the U.S. balance of payments, including merchandise trade, services and transfer payments, and international capital flows. In addition to reporting and analysis of balance of payments statistics, the Office briefs Treasury officials on payments impacts of economic developments and Government policy actions.

The Office also represents the Treasury in interagency, IMF, and OECD technical meetings.

The merchandise trade deficit for the fiscal year was \$30.6 billion, a worsening of \$3.3 billion from the fiscal 1979 deficit of \$27.3 billion.

This slight deterioration was entirely due to world oil price increases in late 1979 and early 1980. The trade balance excluding petroleum imports improved by \$23.2 billion, to a surplus of \$47.9 billion; but petroleum imports rose by \$26.5 billion, from \$52 billion in fiscal 1979 to \$78.5 billion. This increase in oil import costs reflected a 77-percent rise in average oil import prices, partly offset by a 14-percent volume decline.

A considerable weakening of U.S. economic activity during the course of fiscal 1980, compared with our foreign trading partners, caused most of the improvement in the nonpetroleum trade balance. While nonagricultural exports continued to rise strongly (by 26 percent in value and 10 percent in volume), nonpetroleum imports slowed considerably (to a 15-percent value increase with only a 1-percent increase in volume), and actually fell in the second half of fiscal 1980.



Also, agricultural exports, buoyed by a Soviet crop failure and generally strong foreign demand for wheat, corn, and soybeans, increased \$8.6 billion from the previous fiscal year, to \$41.2 billion.

The current-account balance for the fiscal year was in deficit by \$2.1 billion, \$1.9 billion worse than the 1979 deficit of \$200 million. This limited increase in the current-account deficit, despite a larger rise in the trade deficit, reflected a \$1.3 billion increase in the surplus on net invisibles (services and transfer payments). Major changes in service transactions included a \$3.4 billion increase in income on U.S. direct investments abroad (mainly from the oil sector) and a \$3 billion increase in net U.S. payments on military transactions abroad. The net invisibles surplus declined significantly in the third (April-June) quarter, due to a one-time writeoff against direct investment income of nationalization losses incurred by an oil-producing affiliate in the Middle East.

*U.S. current account transactions, October 1979-September 1980*  
[Seasonally adjusted; \$ billion]

	Fiscal 1979 (quarterly averages)	Fiscal 1980*			
		Oct.-Dec. 1979	Jan.-Mar. 1980	Apr.-June 1980	July-Sept. 1980
Exports .....	42.6	50.2	54.7	54.7	56.3
Agricultural .....	8.1	10.4	10.4	9.7	11.0
Nonagricultural .....	34.5	39.8	44.3	45.0	45.3
Imports .....	-49.4	-59.5	-65.6	-62.2	-59.1
Petroleum and products .....	-13.0	-18.9	-21.6	-21.0	-17.3
Nonpetroleum .....	-36.4	-40.6	-44.0	-41.2	-41.9
Trade balance .....	-6.8	-9.2	-10.9	-7.5	-2.8
Net services and remittances .....	7.6	8.3	9.5	5.8	8.6
Government economic grants .....	-9	-9	-1.2	-8	-9
Net invisibles .....	6.8	7.4	8.2	5.1	7.7
Balance on current account .....	-0	-1.8	-2.6	-2.4	4.9

\* Due to seasonal adjustment on calendar-year basis, quarterly data will not add precisely to fiscal year totals.

Source: Survey of Current Business, June and December 1980, published by U.S. Department of Commerce, Bureau of Economic Analysis.

On capital account, the net recorded outflow of private capital nearly doubled from \$22.4 billion in fiscal 1979 to \$42.2 billion in fiscal 1980. The dominant element in this increase was a \$38.4 billion outflow on net banking transactions—of which \$25.3 billion occurred during the third (April-June) quarter, as recession cut into domestic credit demand. The direct investment net outflow declined, from \$16 billion in fiscal 1979 to \$7.5 billion in fiscal 1980, due in part to nationalization effects (during the April-June quarter) on an oil-producing affiliate in the Middle East.

The main source of financing for these and other outflows was a positive statistical discrepancy (presumably due in large part to unrecorded capital inflows) which rose to \$18.7 billion in the April-June quarter alone, and totaled \$43 billion for the year compared with a \$16.2 billion positive discrepancy in fiscal 1979.



Among official capital transactions: Foreign official assets in the United States showed a net inflow of \$7.4 billion for the year; U.S. Government lending increased about \$1 billion from fiscal 1979 to \$4.9 billion; and U.S. reserve assets showed an increase (capital outflow) of \$4.5 billion, partially associated with a \$1.2 billion SDR allocation from the IMF.

*Financing of U.S. current account balances, October 1979–September 1980\**  
[Inflows (+) and outflows (–); \$ billion]

	Fiscal 1979 (quarterly averages)	Fiscal 1980			
		Oct.–Dec. 1979	Jan.–Mar. 1980	Apr.–June 1980	July–Sept. 1980
Current account balance*	—	0.5	–2.4	–0.7	0.5
U.S. reserve assets (increase (–))	–0.1	–.6	–3.3	.5	–1.1
Other U.S. Government assets*	–1.0	–.9	–1.5	–1.1	–1.4
Foreign official assets	1.3	–1.2	–7.2	7.8	8.0
Industrial countries	.6	–6.9	–10.7	3.0	2.4
OPEC members	.5	5.0	2.9	4.7	4.4
Other countries	.2	.7	.6	—	1.3
U.S. banks, net	–.6	–6.8	6.1	–25.3	–12.4
Claims	–10.2	–7.2	–.3	–21.1	–12.5
Liabilities	9.6	.4	6.4	–4.2	—
Securities, net	1.0	.2	4.9	–1.3	–.1
Foreign securities	–1.1	–1.0	–.8	–1.2	–.8
U.S. securities <sup>†</sup>	2.2	1.2	5.7	—	.7
Direct investment, net	–4.0	–1.5	–4.0	–.1	–1.8
U.S. investment abroad*	–6.2	–4.1	–5.7	–3.2	–4.1
Foreign investment in United States*	2.2	2.6	1.7	3.1	2.2
Other U.S. corporate capital, net	–1.0	1.5	–.8	1.5	N.A.
Claims	–1.1	.4	–1.5	.1	N.A.
Liabilities	.1	1.1	.7	1.3	N.A.
SDR allocations	.3	—	1.2	—	—
Statistical discrepancy*	4.0	8.9	7.1	18.7	8.3

\* All data are seasonally unadjusted, because capital flows except U.S. Government lending and reinvested earnings component of direct investment income are not available on seasonally adjusted basis.

N.A. Not available.

<sup>†</sup>Excluding foreign official assets.

Source: Survey of Current Business, June and December 1980, published by U.S. Department of Commerce, Bureau of Economic Analysis.

### Office of International Financial Reports

The Office of International Financial Reports manages two statistics collection systems—the Treasury international capital (TIC) reporting system, and the Treasury foreign currency (TFC) reporting system.

The TIC system collects monthly, quarterly, and semiannual data on U.S. banks' foreign assets and liabilities; U.S. commercial firms' claims on and liabilities to unaffiliated foreigners; and banks' and brokers' securities transactions with foreign residents. These data provide information on all movements of capital between the United States and foreign countries other than direct investment flows and U.S. Government transactions. The TIC staff prepared monthly analyses of foreigners' purchases and sales of U.S.

securities and periodic reports on U.S. banks' lending abroad. During fiscal 1980, the TIC staff also produced regular reports on Iranian assets in and liabilities to U.S. banking institutions.

In addition to providing data on an ad hoc basis to other Treasury offices and Government agencies, the TIC staff supply the capital movement data for monthly publication in the Treasury Bulletin, the Federal Reserve Bulletin, and for quarterly analysis and publication in the Department of Commerce's Survey of Current Business.

The TFC reporting system collects weekly, monthly, and quarterly data on the foreign currency positions of U.S. banks and commercial firms, publishing these data in the Treasury Bulletin monthly. These data, collected under title II of the Par Value Modification Act of 1973 (31 U.S.C. 1141-1143), provide the Government's only information on foreign exchange market positions. During fiscal 1980, the TFC staff negotiated a data exchange agreement with the Comptroller of the Currency to reduce duplicative regulatory reporting by national banks.

#### Office of Data Services

The Office of Data Services provides computer and data processing facilities for the international affairs function within the Office of the Secretary. Data Services also maintains and operates a computerized system for the collection and reporting of information on U.S. Government loans to foreigners.

The Office furnishes computer programming and technical advice services to others, enabling them to efficiently process the large volumes of information analyzed in forecasting the balance of payments and in studying trade and competitive trends, international capital flows, and aid to the less developed countries.

#### Delinquent debt

As of September 30, 1980, the outstanding long-term principal on post-World War II debts, derived mostly from foreign aid and export credit programs of the U.S. Government, totaled \$52 billion. This indebtedness is broken down as follows: (1) \$25.5 billion contracted under the Foreign Assistance Act (and predecessor legislation), (2) \$15.1 billion contracted under the Export-Import Bank Act and the Commodity Credit Corporation Act, and (3) \$8.1 billion contracted under Public Law 480. An additional \$1.3 billion stems from activities directly related to World War II—primarily lend-lease and surplus property disposal programs.

Since World War II, the vast majority of these debts have been paid on time. During fiscal 1980, the United States collected over \$5½ billion of principal and interest payments due on long-term credits, and the equivalent of \$250 million in principal and interest payments on loans repayable in foreign currencies. As of September 30, 1980, principal and interest due and unpaid 90 days or more on post-World War II debt amounted to \$951.5

million. More than two-thirds of this delinquent debt is subject to special political or other factors, as in the case of Vietnam and Cuba, which make prompt payment unlikely at this time.

Foreign outstanding indebtedness to the U.S. Government resulting from World War I totaled approximately \$26.4 billion as of September 30, 1980, of which \$23.9 billion was delinquent. The collection of this debt presents special problems. Most debtor countries fulfilled their commitments under the debt agreements until 1933-34, but have made no payments since. Aside from the Soviet Union, which repudiated all foreign debts in January 1918, the principal debtor governments have never denied the validity of the debts. However, these nations have steadfastly maintained that they would only resume payments on their war debts to the United States on condition that the issue of Germany's war reparations was satisfactorily settled. Resolution of the problem of government claims against Germany arising from World War I has been deferred "until a final general settlement of this matter" by the 1953 London Agreement on German external debts, to which the United States is a party. This agreement was ratified by the U.S. Senate and has the status of a treaty.

As a result of amendments, passed in 1978, to the Foreign Assistance Act of 1961, Treasury's report to Congress on developing countries' external debt and debt relief provided by the United States has been discontinued. However, this information is now provided to Congress in the annual Foreign Assistance Report submitted by the Chairman of the Development Coordination Committee. Part Five of this year's report is comprehensive, containing detailed information on the debt situation of major debtor countries and the means by which the United States and other creditor countries have dealt with debt-service problems.

#### Office of Monetary Research

Major projects undertaken by the Office of Monetary Research in fiscal 1980 included a comprehensive review of the applicability of large-scale multicountry econometric models for policy simulations, assessment of economic benefits derived by the United States from participation in the activities of multilateral development banks, several studies of the international oil market, construction of a detailed financial model of the World Bank, an evaluation of U.S. intervention practices in the dollar/German mark market, a study of worldwide industrial demand for gold, a theoretical investigation into an optimal fiscal/monetary mix of policies under flexible exchange rates, and an appraisal of anti-inflationary macroeconomic policies of other industrial countries.

#### Foreign Portfolio Investment Survey Project

The Foreign Portfolio Investment Survey Project is responsible for the collection and analysis of data relating to international portfolio investment and its effects upon the national security, commerce, employment, inflation,



general welfare, and foreign policy of the United States. The Secretary of the Treasury was designated by the President as the Federal executive responsible for collecting these data mandated by the International Investment Survey Act of 1976 (Public Law 94-472, as amended). The act requires surveys of both foreign portfolio investment in the United States and U.S. portfolio investment abroad.

The task of processing, editing, and tabulating data from a survey of foreign portfolio investment in the United States as of December 31, 1978, was completed in fiscal 1980. A completed questionnaire was required by March 31, 1979, from every U.S. issuer of securities with total consolidated assets of \$50 million if a nonbanking enterprise, or of \$100 million if a bank. However, a firm falling below these asset levels, but with assets of \$2 million or more, was required to report if there was evidence of foreign ownership of its securities. Firms with assets less than \$2 million were exempt from filing a questionnaire. In addition, a questionnaire was required from every U.S. entity acting as a holder of record of domestic securities on behalf of foreign persons if the combined market value of these securities, held for all foreign accounts, exceeded \$50,000 as of December 31, 1978.

The survey data on securities were integrated with information on other types of foreigners' portfolio investments in the United States as reported through the Treasury international capital movements reporting system. The report on this project is scheduled to be completed by the end of calendar 1980.

On November 15, 1979, a study of the need for and feasibility for surveying U.S. residents' portfolio investments abroad was submitted to Congress. Potential benefits of more complete information on U.S. portfolio investment abroad were examined and the costs of collecting information through five different survey options were estimated. The study concluded that the costs to the Federal Government of these five different surveys would range from roughly \$1.5 million for the most limited survey to \$33.4 million for the most comprehensive, feasible sample survey, and that the proportion of U.S. portfolio investment abroad measurable by any given survey effort could not be reliably estimated.

A contract study addressing the collection of information on foreigners' portfolio investment in U.S. partnerships was received in January 1980 and action was initiated to implement its recommendations. The study concluded that the ongoing Treasury international capital movements reporting system does not adequately cover foreigners' portfolio investments in U.S. partnerships and that insufficient information is available to improve the reporting system coverage. In addition, the study suggested that information from U.S. partnership tax returns could be used to estimate the total volume of such investment by foreigners, to identify potential reporters and to design reporting forms if desired. A survey utilizing a sample of U.S. partnership tax returns was designed and Internal Revenue Service cooperation in the effort secured.





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## **ADMINISTRATIVE REPORTS**

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# ADMINISTRATIVE MANAGEMENT

## Management and Organization

The Office of Management and Organization (OMO) advises top officials of the Department and its 11 bureaus on the organizational structures and management systems best suited to carry out their functions. The following were the Office's principal activities during fiscal 1980.

### Organizational changes

*Office of the Secretary.*—OMO assisted in the establishment of the Office of the Special Assistant (Consumer Affairs) whose functions include representing the Secretary on the President's Consumer Affairs Council, chairing the Treasury Consumer Affairs Council, and conducting studies which will lead to more effective and efficient management of Treasury's consumer programs and activities.

The Assistant Secretary (Domestic Finance) was transferred from the supervision of the Under Secretary for Monetary Affairs to that of the Deputy Secretary, and the Fiscal Assistant Secretary was transferred from the supervision of the Under Secretary for Monetary Affairs to that of the Under Secretary.

Two new offices established under the supervision of the Assistant Secretary (Administration) are the Office of Procurement and the Office of the Secretary Equal Employment Opportunity Staff.

Other changes included the transfer of the Office of Audit to the Inspector General, with the accounting and travel policy functions of that office going to the Office of Budget and Program Analysis; and the transfer of the Treasury Payroll/Personnel Information Systems Division to the Office of Management and Organization.

*Departmental.*—The Bureau of Alcohol, Tobacco and Firearms established a new Office of Assistant Director (Planning and Evaluation) to create a central focus for planning, policymaking, and program measurement.

The U.S. Customs Service transferred the support and supervision of the Customs laboratories from the Regional Commissioners to the Customs headquarters. Based on an analysis of workload and other related factors, Customs and OMO developed a plan for redeploying Office of Investigations field personnel.

A major reorganization took effect at the Federal Law Enforcement Training Center (FLETC) on January 1, 1980. The reorganization enhances FLETC's capacity for providing students with the most current information on and techniques used in law enforcement.

### Special projects

*Office of the Secretary.*—A senior analyst led the development of a merit pay system for the Office of the Secretary and eight Treasury bureaus. The system has two unique features. First, a salary table is used, with a finite number of salary increments, rather than a salary band or range. Second, the pay change computation system uses a formula which takes into account the overall performance rating distribution as well as individual performance ratings. This feature inhibits rating inflation.

OMO directed a study of the use of word processing equipment in the Office of the Secretary. This study made a number of recommendations for



short-term improvements and provided a basis for determining the budget impact for word processing equipment.

A senior analyst acted as Special Assistant to the Secretary (Consumer Affairs) until the position was filled permanently. This involved assisting in the preparation of Treasury's consumer program plan and consumer directive. These documents laid the foundation for consumer input into Treasury policymaking processes.

Staff offices under the Inspector General and the Assistant Secretary (Administration) prepared orders and directives which extended the authority of the Inspector General in integrity-related matters.

*Departmental.*—A senior analyst chaired a task force which assisted the Bureau of Government Financial Operations (BGFO) in making improvements in its check claims operations.

OMO also assisted the Assistant Secretary (Administration) in assessing BGFO's needs to replace computers at its disbursing centers and to evaluate a management consultant's study dealing with the optimum number of disbursing centers.

A space-use study in the Bureau of Engraving and Printing examined and assessed current requirements, assessed the need for additional space, and developed a plan for effective utilization of currently occupied space.

OMO assisted the Assistant Secretary (Administration) and a task force of top administration officials from each bureau in defining policies, procedures, and issues which adversely affect the morale of senior career employees. A report suggesting remedial actions was produced.

OMO participated in an Office of Management and Budget debt collection project which reviewed the activities of Treasury bureaus. The study addressed such areas as the billing system for supplemental duties, fines and penalties, and interest on delinquent accounts.

#### Continuing management programs

*Zero-base budgeting objectives.*—During fiscal 1980, all Treasury bureaus submitted ZBB objectives and participated in periodic progress review sessions with their policy supervisors and other policy and staff officials. Key fiscal year operating objectives were defined, expected accomplishments set, and specific milestones identified for tracking during the year.

*Advisory committee management.*—One new advisory committee was established and two charters were renewed during the year. It was recommended that a Presidential advisory committee managed by Treasury be continued by Executive order.

*OMB Circular A-76.*—New Treasury instructions were developed to implement revised OMB Circular A-76 concerning contracting for commercial and industrial goods and services.

*Productivity management.*—OMO continued to work with the bureaus to improve their productivity programs. Departmental coverage in the Federal productivity measurement system increased to 82 percent. A major effort to revise productivity measures was undertaken in the Office of the Comptroller of the Currency.

*Departmental information resources management program.*—During fiscal 1980, the Departmental Information Resources Management Staff initiated programs aimed at reducing postage costs, reducing the size of records holdings, and easing recordkeeping requirements imposed on the public.

An automated Treasury information locator system (TILS) was established to eliminate duplicate information requirements. TILS will eventually identify all public, interagency, and congressional reports, and departmental

forms and permit quick access to this information. In the same vein, a program for control of internal reporting requirements was initiated.

The first annual Information Collection Budget was compiled on all of Treasury's current and projected public reporting requirements and submitted to the Office of Management and Budget for approval.

*Assistance to international visitors.*—The International Visitors Program office provided a wide variety of appointments and programs in the Office of the Secretary and bureaus for 138 visitors from all parts of the world referred by the International Communication Agency and other organizations. In addition, the office arranged meetings for three groups of international visitors and eight classes of junior Foreign Service officers.

#### Financial management

The accomplishments of the Financial Management Division during fiscal 1980 included the conversion of the time and attendance records from manual to terminal processing and major gains in automation of the budget execution and reporting system. An appropriation for the administrative expenses of the Chrysler Corp. loan guarantee program was added to the responsibilities of the Division. In addition, the administrative expenses for international programs formerly funded by the Exchange Stabilization Fund became a separate international affairs appropriation. The Division is now responsible for 11 accounts.

#### Treasury payroll/personnel information system

Due to a change in management of the Treasury payroll/personnel information system (TPPIS), improved emphasis is being placed on user services, responding to user needs, and improved scheduling for supporting operations.

Sessions for the retraining of user employees, scheduled and conducted periodically throughout the processing year, have preceded a marked reduction in error rates and processing problems from participating agencies and their employees. Currently, to further reduce errors, 80 percent of the participating agencies have been converted to automated time and attendance processing. The remaining 20 percent of accounts are scheduled for conversion in early fiscal 1981.

A data retrieval package was installed in TPPIS in the last quarter of fiscal 1980. During the coming year, this service will be available to all participating agencies, allowing them to retrieve data and create reports unique to their needs directly from the TPPIS data base and receive these reports through the telecommunications interface in their local equipment.

#### Budget and program analysis

The Office of Budget and Program Analysis continued to develop policies and procedures and to direct and coordinate the formulation, justification, and presentation of budget levels which totaled over \$95 billion in fiscal 1980. The amount includes \$3.6 billion for operating appropriations, \$74.7 billion for public debt and other interest, and miscellaneous accounts, \$17.7 billion for the Energy Security Corporation, and \$6.9 billion for general revenue sharing. In addition, the Office initiates selected analytical studies designed to systematically measure the achievements of bureau programs with stated objectives.

During fiscal 1980, the budget staff—

1. Maintained controls on expenditures, number of personnel on roll, reprogramming activities of each Treasury bureau, and uses of appropriated funds as specified by departmental, OMB, and congressional policy.

2. Gave special budgetary consideration and emphasis, including the preparation of requests for budget amendments, supplemental appropriations, and reimbursements, to programs of special concern to the administration. These included the supplementals for the 1980 Presidential candidate and nominee program in the Secret Service, increased costs related to issuing and redeeming savings-type securities in the public debt, and amounts related to the new refundable energy credit allowed for solar/wind conservation investments by businesses.

3. Obtained supplemental appropriations for the cost of pay increases authorized by Executive Order 12165, wage board actions, and administrative actions amounting to \$127.4 million. A total of \$40.4 million of the increased costs was absorbed by application of program savings, reimbursements, and use of budgetary reserves.

4. Updated instructions for the Treasury Financial Resource Management System (spring budget process) which called for the submission of new requirements in fiscal 1982, in accordance with departmental target levels and program guidance.

5. Assisted in the preparation and presentation of budget requests for funds totaling \$3.688 billion to be appropriated to the President for the U.S. share to the multilateral development banks, of which the Secretary of the Treasury serves as a Governor.

6. Established elaborate control systems for monitoring the congressionally mandated travel reduction and Presidential hiring restrictions.

7. Implemented a new full-time equivalent employment control system for startup in fiscal 1981. Treasury will be participating in a test with nine other agencies and departments before Government-wide implementation in fiscal 1982. The purpose of the new system is to replace the existing "one day" employment ceiling with a work-year ceiling more closely tied to resource levels.

During fiscal 1980, the Program Analysis Staff conducted the following studies:

1. Assessed the causes of inventory backlog in the Bureau of Government Financial Operations, Division of Check Claims, and evaluated the action plan and management objectives designed to correct the deficiencies.

2. Reviewed the size and history of the reimbursed functions performed by the U.S. Customs Service for the U.S. Department of Agriculture and examined policy issues regarding agricultural inspections.

3. Made recommendations for determining the most efficient and cost-effective method of securing commercial services to the Office of Administrative Programs.

4. Compiled a compendium of program evaluations conducted by the Department of the Treasury between July 1, 1978, and June 30, 1979.

5. Assisted in providing the Office of the Secretary with a merit pay plan in accordance with Office of Personnel Management guidelines.

6. Recommended that Public Debt seek to satisfy requirements for savings bond stock through competitive procurement.

In February 1980, the Office assumed responsibility for the accounting and travel policy for the Department. During 1980, the Accounting and Travel Policy Staff—



1. Provided support to TPPIS through monitoring and development of the design documentation. On September 30, 1980, the TPPIS design was approved by the Comptroller General of the United States.

2. Monitored the U.S. Customs Service appropriation/cost accounting system design.

3. Prepared delegation of authority to heads of bureaus to approve or authorize use of first-class accommodations, use of noncontract carriers, and questionable payments of \$25 or less.

#### Personnel management

Fiscal 1980 was a period of continuation of effort directed toward implementation of the Civil Service Reform Act (CSRA). Many program modifications and improvements unrelated to civil service reform were also implemented.

Treasury's Senior Executive Service (SES) member and candidate development program was established by the departmental Executive Resources Board. Approximately 45 SES candidates were selected for this program.

The first performance appraisals under the CSRA were completed for over 500 of the Department's executives. The President recognized 17 of these executives for their sustained accomplishments by conferring on them distinguished and meritorious executive rank awards.

All implementation items required by title VII of the CSRA were completed. The Department reviewed and approved a number of agreements negotiated for the first time under the act. Action was also initiated to seek clarification and interpretation of certain sections of the act through reference to interpretive litigation. Policy and procedures were developed to implement those provisions pertaining to performance appraisal, adverse actions, and actions against employees based on unacceptable performance.

Treasury continues to be the highest unionized Cabinet-level agency in the Federal Government. Fifteen different unions represent nearly 100,000 employees in 9 bureaus and in the Office of the Secretary. This represents nearly 84 percent of the Department's total employment.

Approximately 90 Treasury employees (GS 1-8) are participating in the Career Development Program for Lower Level Employees (CADE). To support this program, a counseling package entitled "CADE Counseling for Federal Careers" was developed.

Departmental and bureau Federal equal opportunity recruitment programs were developed. A position of personnel psychologist was established to spearhead the Department's program and oversee bureau activities in implementing the uniform guidelines on employee selection procedures.

Bureau staff developed a computerized system to facilitate direct contact with national, regional, State, and local minority, female, veteran, and handicapped organizations. The recruitment resources information system identifies thousands of such organizations willing to assist the Department and other Federal agencies in their recruitment efforts.

Treasury participated in a Department of Labor/OPM migrant worker trainee program, with training funded by CETA. Upon completion of training, individuals will be employed in clerical capacities. Treasury, with 35 individuals to be employed, has the second highest participation in Government.

Treasury also participated in a project to develop evaluation procedures for possible use as an alternative to the Professional and Administration Career Examination (PACE) in filling positions of revenue officers, tax technicians, and customs inspectors. This project is targeted for completion in 1983.



Six Presidential management interns were trained by the Department in fiscal 1980. Those trained in 1978 were converted to permanent status.

The number of critical-sensitive positions was reduced significantly in three bureaus and the Office of the Secretary. These positions will no longer require full-field investigations. This also resulted in reducing the number of security clearances.

Merit pay systems covering about 55 percent of employees in grades GS 13-15 were developed. The remainder will be developed and implemented by the statutory deadline date of October 1981.

The Department negotiated with the Office of Personnel Management an agreement delegating to Treasury 13 specific personnel authorities made available to agencies on an optional basis. These include the authority to approve certain appointments at pay rates above the minimum, to establish Schedule C positions within the Department's quota, and to approve waiver of time-in-grade restrictions.

#### Procurement management

In fiscal 1980, the Office of Procurement was established in the Office of the Assistant Secretary (Administration). The procurement staff, formerly in the Office of Administrative Programs, was assigned to the new office, divided into three organizational elements: Departmental Procurement Management Staff, Saudi Arabian Procurement Support Staff, and Office of the Secretary Procurement Division.

Total commercial procurements for the Department in fiscal 1980 totaled \$380 million, which excludes contracts funded by the Saudi Arabian Government. Of the total amount, \$292 million was expended through Treasury negotiated and advertised contracts, with the balance being ordered under established General Services Administration and other agency contracts. To assist Treasury bureaus in increasing their contract awards to small businesses, minority firms, those in labor surplus areas, and women-owned firms, the Office of Procurement has obtained access to the Small Business Administration's computer data base to identify such firms for bureau bidders' mailing lists.

During fiscal 1980, the negotiation of 35 blanket purchase agreements by the Office of Procurement for use by all Treasury bureaus provided a savings in excess of \$92,000 over standard unit prices under existing Government contracts. The Department-wide consolidation of Treasury requirements for 657 law enforcement vehicles procured through GSA and in excess of 15 million rounds of small-arms ammunition resulted in a significant dollar savings over separate procurement methods. Compacts, intermediate- and full-size automobiles, and 27 types of ammunition were purchased.

Major Office of the Secretary contracts included professional services in support of the New York City and Chrysler Corp. loan programs and a major computer system. The last contract was awarded competitively in the amount of \$8.6 million over a systems life of 6 years.

The Department continued its staff assistance visit program to the bureaus to help identify potential for improvement in Treasury's overall contracting activities. Visits were made to five bureau headquarters and five regional cities, each of which contained several bureau procurement offices. Reports of findings and recommendations were issued to bureau officials, with a requirement of corrective action within 90 days.

In support of the U.S. technical cooperation agreement with the Saudi Arabian Government, Office of Procurement contract specialists, using Saudi funds, awarded and administered contracts in excess of \$35 million in fiscal

1980. In addition, a major competitive contract in the amount of \$23 million was awarded by the Office of Procurement for construction of the Royal Saudi Power Station in Riyadh.

Treasury continued its participation in vendor procurement conferences during fiscal 1980. Departmental personnel or bureau personnel designated to be the Department's representatives attended 25 conferences throughout the Nation to provide information to small businesses and minority vendors interested in selling to Treasury. Additionally, an outreach program was initiated in the Washington, D.C.-Maryland-Virginia area to advise women-owned business firms how to do business with Treasury bureaus and to inform them of the Department's efforts to increase its contract awards to women-owned firms.

#### Emergency preparedness

The Emergency Preparedness Staff directed primary emphasis to the continuing enhancement of the Department's overall emergency preparedness posture. Improvement was achieved through program review and evaluation, participation in interagency projects, task forces, and civil readiness exercises. It is essential that Treasury's contingency plans be developed in keeping with changing concepts and technologies, and in anticipation of potential crises. To this end, a close working relationship was maintained with the Federal Emergency Management Agency and other departments and agencies with emergency preparedness responsibilities under Executive Orders 11490 and 12148. Participation in major interagency activities included studies directed by the National Security Council on Continuity of Government and Mobilization Planning and Programming; Cooperative Postwar Recovery Analysis (COPRA); development of a Federal Master Mobilization Plan; and Civil Readiness Exercises REX-80 ALPHA (March 1980).

In preparation for Treasury's participation in REX-80 ALPHA, the Division Director coordinated a meeting involving the Defense Intelligence Agency, the Studies, Analysis and Gaming Agency, and the Treasury Office of Intelligence Support for the presentation of a politico-military background briefing for members of the three Treasury emergency executive teams. The multiphase briefing provided a hypothetical nuclear war illustration, comparison with the current world situation, and Treasury's emergency preparedness responsibilities and requirements. It provided an excellent means for team members to become more aware of possible national emergency situations and Treasury's role therein.

The readiness posture of the national and departmental programs was enhanced through interagency development of the Federal Master Mobilization Plan and responsible agency implementing plans. These plans will be tested in REX-80 BRAVO, a national-mobilization-type exercise, scheduled for early fiscal 1981.

The Department's standby readiness posture commands continuing attention for keeping current emergency executive team lists and maintenance of the emergency operating facilities. In this regard, the staff is prepared to activate and operate the Treasury emergency operating facility on short notice with the relocation of an emergency cadre.

#### Physical security

A departmental directive that established policy, reporting responsibility, and procedures for the development and maintenance of the Department of the Treasury data index system was promulgated. The directive prescribes

that any document originating within the Department and assigned a national security classification of Top Secret, Secret, or Confidential be entered into the system, providing for better management and control of classified information.

The Department's Foreign Government Information Guidelines were developed and provided to the Information Security Oversight Office. They provide guidance and procedures for the uniform systematic review of declassification of 30-year-old foreign government information. Unless declassified earlier than 30 years, such information is to be reviewed for declassification no later than 30 years from the date of origin.

In compliance with the mandate of Executive Order 12065, an orientation and training program was developed to familiarize departmental personnel with the pertinent provisions of the order and the Department's implementing regulation regarding the handling and safeguarding of classified national security information. This program has been proffered to each Treasury bureau for specific adaptation.

#### Property management

During fiscal 1980, Treasury personal property transactions included the reassignment within Treasury of property valued in excess of \$418,000. Personal property valued in excess of \$13.8 million, no longer needed by Treasury, was reported to GSA for transfer to other agencies, donations, or sales auction. Treasury also obtained, without cost, personal property valued at over \$20 million from other Federal agencies.

Space planning initiatives to consolidate bureau headquarters activities have been severely hampered for the second straight year by the current leasing and tight rental market in Washington, D.C. The continuing abnormal number of expiring leases, combined with renewal rights not being extended to the Government, causes continued fragmentation and has limited to two the total reduction in locations within the past year. The Office of the Secretary occupies 14 of 56 locations, including 2 storage facilities. A study of the long-range headquarters space needs of the Secret Service has received departmental approval and has been submitted to GSA for implementation. Additionally, departmental approval has been given to expand the Service's specialized training programs at Beltsville, Md. The development of a facility master plan to accommodate the new training initiatives has been undertaken with GSA. Implementation approval is being withheld pending design completion and costing of the plan.

GSA completed the open office planning for the Office of Revenue Sharing at Columbia Plaza in March 1980. Planning for this project was initiated in April 1976. Construction of this project was accomplished in five phases over a period of 2½ years.

The Main Treasury repair and improvement program is progressing:

1. Construction has been completed on a \$2 million project to replace the primary electrical system, and the fire, security, and civil defense alarms.
2. Structural repairs to the roof's balustrades and cornices have been completed. Additionally, major repairs to the main building roof, which secures the water-tight integrity, were completed as a part of this contract.
3. Structural repairs to the south corridor basement floors have been completed. The remaining basement corridors will be repaired in future contracts as yet unscheduled.
4. Design work for the installation of computers in prior vault space was completed and construction is underway. Total project completion is scheduled for the end of 1980.



5. Contracting for an energy analysis study of the facility is underway.

6. Design work to replace the primary electrical system in the Treasury Annex is underway with completion of the installation scheduled for September 1981.

7. Design work for installation of an emergency generator system was completed. As a result of escalating construction costs, the project scope is being drastically reduced to permit the use of two small generators recently made available to the Office of the Secretary.

8. Design work on the project for air conditioning renovations, secondary electrical distribution, window repairs, and downspout and rainleader repairs was deferred to accommodate the design effort.

#### Printing management

Fiscal 1980 included renewed efforts to realign the departmental printing plant to more efficiently and economically expedite the types of work for which the plant was established. Actions taken included the reduction of seven working capital fund positions and the surplusing of seven items of conventional printing equipment. To maintain production, a Xerox 9500 duplicator, a much less labor-intensive piece of equipment, was leased. The departmental printing plant as currently equipped and staffed is able to produce work for the Department faster and more efficiently than prior to fiscal 1980.

The current administration's increased concern over the inflation/recession situation of the country has stepped up the visual reporting requirements of the Office of the Secretary. Because of this, the Graphics Branch has experienced a marked increase in the number of requests for statistical data to be charted and reproduced in the form of colored vu-graphs and 35mm slides to be used at briefings of the Secretary and his staff. The production of these visual efforts has been determined to be the most comprehensive and accurate method of presenting the data.

The Printing Procurement Branch designed a unique dual-purpose self-mailing order form and pocket poster introducing the two gold medallions in a 5-year series issued by the Department of the Treasury under the American Arts Gold Medallion Act to commemorate outstanding individuals in the American arts. Order forms and posters were printed in four colors and were distributed to 37,000 post offices in the United States and its territories where they are readily available to the public.

A Printing Management official chaired a task force that investigated the feasibility of procuring from commercial sources the alcohol strip stamps currently produced by the Bureau of Engraving and Printing for the Bureau of Alcohol, Tobacco and Firearms. The final decision was to continue to produce the strip stamps in-house at the Bureau of Engraving and Printing. However, as a direct result of the work of the task force, significant changes in the stamp manufacturing program took place which will result in savings of over \$2 million annually.

Representatives of Printing Management attended two of a series of meetings being hosted nationwide by the staff of the Joint Committee on Printing (JCP) and representatives of the Government Printing Office (GPO) with printing officials from Government, private industry, and the library community. The meetings were designed to discuss JCP and GPO policies and programs, and to solicit comments and feedback from the participants. The meetings were held in Chicago and Atlanta, the sites of two of Treasury's authorized printing plants.



### Telecommunications

*Treasury Centrex telephone system.*—The Treasury Centrex system has been in service for nearly 4 years and now serves Treasury bureaus and 2 other Government agencies with over 18,000 telephone stations. An automated directory and information service was implemented in 1980. The use of the single-line telephone in lieu of the more expensive multiline telephones or call directors is progressing well and is expected to result in significant savings.

*Long-distance telephone cost reduction program.*—Treasury continued its efforts to reduce long-distance telephone costs in both the Federal telecommunications system (FTS) and commercial calling. In fiscal 1980, Treasury reduced its calling volume by nearly 500,000 calls below its quota and received compensation equivalent to \$400,000. Efforts will be continued during the coming year to use detailed calling data and FTS off-net restriction capability to hold down long-distance telephone costs.

*Communications security program.*—The Treasury communications security program has made significant improvements in the security and protection of Treasury economic and law enforcement information. During the past year, substantial progress was made in providing secure telephone service for Treasury overseas attaches. Secure telephones are now in place in many key overseas foreign service locations for the use of Treasury personnel and other members of the foreign affairs community.

*Overseas telecommunications support.*—The United States-Saudi Arabian Joint Commission on Economic Cooperation has sponsored projects within Saudi Arabia being managed and implemented by public and private U.S. organizations, including Federal agencies. Each of the projects requires communication with parent organizations in the United States, and several require data processing support as well. To satisfy these basic requirements, a private Treasury satellite telecommunications network has been developed and installed by Telecommunications Management. Also, an intra-Saudi-Arabian information network interconnecting research facilities throughout the Kingdom is planned.

### Paperwork management

*Office of the Secretary paperwork management program.*—Five new records control schedules for three major offices were developed, permitting disposition of more than 6,000 cubic feet of records.

A new reports management program to convert an existing manual retrieval system to an automated system is 50 percent complete. It is organized into four categories: Internal (Office of the Secretary and departmental), GAO/legislative, public use, and interagency.

### Facilities services

*International support.*—The Facilities Services Division provided administrative planning and coordination for U.S. delegation visits led by Treasury to several Mideast countries, Germany, and Brazil. The Division also planned and coordinated administrative support for the U.S. delegation attending the IMF/IBRD annual meetings in Washington, D.C., and the Secretary's reception in honor of IMF/IBRD Governors held at the National Gallery of Art.

### Environmental programs

*Environmental quality.*—Two directives were issued to implement the Council on Environmental Quality regulations for the National Environmen-

tal Policy Act and Executive Order 12114. The Assistant Secretary (Administration) approved environmental assessments concerning the Customs Detector Dog Training Center, proposed production equipment for the Bureau of Engraving and Printing, environmental reviews in connection with a new computer center in the Main Treasury Building, and a study of the New York Assay Office.

*Historic preservation.*—Treasury continued its participation as a statutory member of the Advisory Council on Historic Preservation. This included the review of studies and proposed procedures regarding Federal undertakings involving historic properties. The Treasury historic preservation directive is being revised in accordance with the Council's new regulations on the National Historic Preservation Act.

*Energy conservation.*—The Under Secretary of the Treasury and the Assistant Secretary for Conservation and Solar, Department of Energy (DOE), participated in the presentation of Treasury energy conservation certificates of appreciation to the Customs Service and the Federal Law Enforcement Training Center in recognition of the awarding of 29 grants, totaling \$863,930, under DOE's solar in Federal buildings program. The solar systems, once installed and operational, will reduce Treasury's energy costs and, more important, its reliance on nonrenewable energy sources. A DOE solar energy award banner was also presented to Treasury.

A task force was established to develop and implement a departmental drivers energy conservation awareness training program plan which will include behind-the-wheel instruction for an estimated 20,000 drivers. Such instruction has yielded fuel savings of 6 to 14 percent on the part of trained drivers. An interagency agreement between DOE and Treasury will provide \$90,000 for the purchase of six electric vehicles for use by FLETC.

#### Information services

*Library.*—To better control materials loaned from the Treasury library collection, an automated circulation system has been developed and put into operation. Expansion of the microforms collection to save space and preserve deteriorating materials is continuing. At the present time, the collection includes more than 8,000 reels of microfilm and over 200,000 microfiche, roughly equivalent to 50,000 hard-bound volumes, but occupying less than 1 percent of the space that would be required to house paper copies. Planning is underway for conversion of all library catalog data to machine readable form. The addition of a legal data base service enhances the automated reference services available to Treasury officials and staff using the library.

*Disclosure Branch.*—With the addition of a Privacy Act officer, the Disclosure Branch was able to substantially increase the scope of its activities. A review of the systems of records covered by the Privacy Act is being undertaken in the Office of the Secretary, which should result in a reduction of records systems. A revised departmental regulation and directive, explaining procedures to be followed in administering the provisions of the Freedom of Information and Privacy Acts, has been prepared.

#### Safety

*Office of the Director of Safety.*—Extensive coordination and planning went into preparation for compliance with Executive Order 12196, "Occupational Safety and Health Program for Federal Employees," which becomes effective October 1, 1980.

The disabling-injury frequency rate (number of disabling injuries per million staff-hours) rose slightly, from 5.5 percent in calendar 1978 to 5.7 percent in calendar 1979.

*Treasury Occupational Safety and Health Council (TOSHC).*—The Council held its 24th annual meeting on June 17, 1980, in Treasury's Cash Room. In conjunction with the meeting, there were safety and occupational health displays and the announcement of a 2-year Treasury safety and health campaign. The Secretary of the Treasury spoke to the assembly, and the Director of the Mint gave the featured address. Other presentations were made by the Director of Consumer Participation, National Highway Traffic Safety Administration, and the Deputy Director of the Occupational Safety and Health Administration's Office of Training, Education, Consultation and Federal Agency Programs. The 32d Annual Report of Safety Progress for 1979 was distributed to the 160 people in attendance.

#### Treasury Historical Association

During fiscal 1980, the Treasury Historical Association held a membership meeting at which Joseph Grano spoke on the history of Rhodes Tavern and urged the members to write letters to appropriate public figures in a last-ditch attempt to save the building.

A portrait of Michael Hillegas, the first Treasurer of the United States, was donated to the Association by the estate of the late Wesley T. Hammer and is being displayed in the office of Azie Taylor Morton, the present Treasurer. The Association was also presented with a portrait of former Secretary W. Michael Blumenthal at a ceremony attended by many dignitaries and followed by a reception in Mr. Blumenthal's honor.

The Association began its pilot oral history program with an interview, conducted by Dr. Richard Schick, with former Secretary of the Treasury John W. Snyder, who served under Harry S. Truman. Two copies of the transcript, over 70 pages long, have been deposited in the Treasury library, a third has been sent to the Truman Library in Independence, Mo., and it is available to the public.

Officers are Charles E. Walker, Chairman of the Board; Robert B. Burrill, President; Christine F. Ligoske, Vice President; Ellen Stockdale, Secretary; John J. Benvegar, Executive Secretary; and Laura L. McAuliffe, Treasurer. There are 335 members.

## BUREAU OF ALCOHOL, TOBACCO AND FIREARMS

The Bureau of Alcohol, Tobacco and Firearms (ATF) regulates the industries and enforces the laws dealing with alcohol, tobacco, firearms, and explosives.

During fiscal 1980, ATF collected approximately \$8 billion in Federal alcohol and tobacco excise taxes. Investigations of trade practice violations were made to ensure free and open competition in the alcoholic beverage industry. Actions were initiated to increase voluntary compliance with Federal alcohol regulations. The Bureau moved to alert pregnant women that excessive alcohol consumption may cause fetal damage; to increase production of alcohol for use as a fuel additive (gasohol); to update alcohol



advertising and trade practice regulations; and implement consumer-oriented wine labeling regulations.

ATF expanded its explosives enforcement program in fiscal 1980. National response teams were formed to respond immediately in major explosives incidents believed caused by bombing or arson. Arrests rose through arson task force efforts in major metropolitan areas.

The development of explosives taggants moved ahead. Taggants, when perfected, provide a method to trace the source of explosives after detonation and to locate explosives before detonation.

The Bureau continued leadership in a Federal-State program to curb interstate cigarette smuggling. Cigarette smuggling defrauds State and local governments of tax revenue and is a multimillion-dollar criminal enterprise. ATF worked in partnership with State and local authorities to arrest smugglers and seize untaxed cigarettes.

### **Criminal Enforcement**

ATF criminal enforcement programs in fiscal 1980 centered on major, complex violations involving firearms, explosives, and contraband articles. Priority was given to assisting State and local governments hampered by limited resources or jurisdictional restraints. ATF made 3,541 referrals of enforcement data to State and local authorities.

Investigations initiated in fiscal 1980 involved 12,193 suspects; investigations of 10,678 suspects were completed; 1,097 defendants were recommended for prosecution; and 697 defendants were convicted. The investigation of explosives crimes remains ATF's top enforcement priority. The Bureau continued to investigate and apprehend violators who traffic in illicit firearms, and placed emphasis on curbing violators who supply firearms to organized crime. ATF also is involved in suppressing interstate traffic in smuggled cigarettes and holding criminal activity to a minimum in the area of alcohol enforcement.

#### **Explosives enforcement**

Criminal misuse of explosives in fiscal 1980 led to 1,751 investigations initiated nationwide by ATF. ATF developed 2,342 suspects in explosives investigations; 363 defendants were recommended for prosecution; and 191 were convicted. Explosives, used illegally and improperly, caused 41 deaths, 209 injuries, and over \$12.6 million in property damage.

A record of explosives thefts and recoveries was compiled by ATF through the use of a computerized system. A toll-free telephone number provides direct contact between citizens and ATF field offices. An "Annual Explosives Report," containing detailed data on explosives incidents, was distributed to law enforcement agencies in this country and abroad.

In fiscal 1980, 197,931 pounds of explosives and 79,780 blasting caps were reported stolen. ATF and other law enforcement agencies recovered 123,236 pounds of explosives and 33,564 blasting caps.

Following are a few examples of the type of bombing cases the Bureau was involved in over the past year:

Four individuals were arrested following a joint investigation conducted by ATF and the Postal Inspection Service into the bombing of a building in Harrisburg, Pa. The owner of the building and his attorney were also charged with conspiracy and mail fraud.

ATF special agents in Boston concluded an investigation of an explosion that completely destroyed a building by the use of an improvised timing



device designed to ignite natural gas. The explosion damaged an additional 68 businesses and injured 23 persons. The owner of the property was arrested in connection with the profit-motivated crime.

ATF special agents in Tennessee culminated a 1-year investigation with the arrest of three defendants for violations relating to the arson and attempted bombing of a nightclub in Nashville, Tenn. The agents found a bomb which contained 180 pounds of high explosives wired by a timing device. The bomb was one of the largest car-bombs discovered in the United States.

#### Arson enforcement

In fiscal 1980, 667 arson investigations were initiated which involved 752 suspects.

ATF pioneered the concept of the arson task force, which combines the resources of Federal, State, and local arson investigators. The ATF arson task force in Houston, Tex., concluded a 15-month investigation which led to the life imprisonment of a member of a New Jersey organized crime family. He was the alleged leader of a major "arson-for-hire" ring responsible for numerous fires to businesses and homes in the Houston area.

In Alaska, five men were indicted for destroying, by arson, the International Market Place in Anchorage. Damage to the contents and building structures was estimated to be approximately \$3.8 million.

ATF arson training was administered to approximately 385 State/local personnel in 7 cities as well as to 200 ATF personnel at the Federal Law Enforcement Training Center in Glynco, Ga.

#### Firearms enforcement

Firearms enforcement was directed toward curtailing the flow of firearms to criminal elements. Firearms investigations encompassed 12,401 suspects in fiscal 1980; 1,346 investigations involved organized crime figures; 602 related to illicit international arms traffic and were conducted jointly with the Customs Service; and 1,334 were investigations of interstate firearms thefts. In fiscal 1980, 694 individuals were convicted for violations of Federal firearms laws.

ATF directed significant support to firearms enforcement programs at the State and local levels, in keeping with the congressional mandate of the 1968 Gun Control Act.

One example of ATF assistance to State and local enforcement agencies is the initiation of a Law Enforcement Assistance Administration (LEAA)-funded training program for State and local officers in firearms investigation techniques to be given in 18 cities.

Some significant firearms investigations conducted by the Bureau in fiscal 1980 are as follows:

A 1-year joint task force between ATF agents and the Department of Justice against the Hells Angels Motorcycle Club in Northern California originally indicted 33 persons. Related cases have resulted in indictments of 19 others on ATF/Drug Enforcement Administration (DEA) charges. Over 180 firearms were seized.

One investigation involved a firearms trafficking ring which purchased over 800 handguns in the Youngstown, Ohio, area for distribution to New York City. Four persons were arrested and to date two have been convicted.

Another investigation documented the purchase of 197 handguns from various sources in Ohio for subsequent distribution in New York City. Three persons have been arrested. One of the weapons purchased was used in the attempted murder of a New York City police officer.

A Newark, N.J., suspect surrendered to ATF agents and was charged with manufacturing .25-caliber penguins, which were then distributed throughout the New York/New Jersey area. This arrest culminated a 3-month undercover investigation in which 151 penguins were purchased in New York City. Two separate undercover seizures involved 1,000 penguins in this same area. A total of five other suspects have been charged in the investigation involving two other Newark residents.

Another major investigation involved the manufacture and distribution of MAC-10 machineguns throughout the United States and particularly the Miami metropolitan area, where nine drug-related homicides have been committed with these weapons since 1979. In fiscal 1980, ATF agents served a series of Federal search warrants in the Tampa area which resulted in the seizure of 480 machineguns and 224 silencers as well as documenting the illicit manufacture of almost 2,000 of these weapons.

The Bureau has initiated a new firearms enforcement strategy in which emphasis is directed at firearms violations by members of organized crime, members of extremist groups, firearms traffickers, and DEA Class I narcotics traffickers dealing in large quantities of firearms. These violations are considered Class I violations and will receive top priority within the firearms program.

#### **Cigarette smuggling**

ATF received enforcement responsibility for the Federal contraband cigarette statute, Public Law 95-575, on December 5, 1978. The law enabled ATF to assist State and local authorities in cases involving interstate cigarette smuggling activities which defraud State and local governments by evading tobacco excise taxes.

ATF's cigarette enforcement program is directed at assisting State enforcement and revenue agencies in their efforts to collect all cigarette taxes set forth by statute and combating contraband cigarette traffic in areas beyond the States' jurisdictional and resource capabilities. In 1980, ATF's enforcement efforts to deter cigarette smuggling in conjunction with State agencies resulted in the seizure of 106,801 cartons of contraband cigarettes and 79 arrests.

ATF studies of the legal and illegal nationwide cigarette distribution system has provided important information. Over-the-road smuggling of cigarettes from low-tax-rate States to high-tax-rate States is not as significant as once thought. The greatest potential sources of tax diversion occur at the stamping agent level. As a result, ATF and the National Tobacco Tax Association have initiated a program to encourage all States to use the Schedule C reporting procedure which verifies interstate shipments of cigarettes by interstate stamping agents.

For fiscal year 1980, cigarette tax collections in those 17 States previously identified by the Advisory Commission on Intergovernmental Relations as experiencing significant cigarette revenue losses have collectively increased \$67 million over the previous tax year. The most significant gains were experienced by Florida, \$19.2 million; Texas, \$16.2 million; and New York, \$10 million. Significant increases in each of these States can be directly attributed to ATF/State enforcement efforts directed at combating contraband cigarette trafficking.

ATF has provided contraband cigarette smuggling training to five schools representing training for approximately 195 students with the use of LEAA funding. The training should further assist in encouraging a cooperative working relationship between ATF and State/local agencies. Through the

cooperative efforts of ATF, the State of Florida was provided a grant from LEAA to form a State tobacco task force, to be assisted by ATF, in identifying and combating cigarette smuggling into the State.

Some selected smuggling cases are as follows:

ATF special agents and New York authorities executed seven warrants in the New York City area, charging six members of the Gati-Legrano smuggling groups with racketeering, conspiracy, and cigarette smuggling. A second indictment charged an independent smuggler with the same charges. The Gati-Legrano operation was charged with smuggling over 2 million cartons of cigarettes into New York between 1977 and 1980, resulting in a tax loss to the State and city of New York of over \$5 million.

Another case involved the arrest of an individual in New Jersey, who had in his possession 767 cartons of cigarettes with North Carolina stamps. This arrest was the culmination of a mobile surveillance that originated in North Carolina, and involved personnel of the Charlotte, Richmond, Falls Church, and New Jersey districts.

A joint investigation between ATF and Massachusetts authorities resulted in the arrest of an individual found to have 360 cartons of New Hampshire and nonstamped cigarettes in his car and 1,140 cartons of nonstamped cigarettes in his home.

ATF special agents and Maryland authorities arrested an individual and seized 1,003 cartons of contraband cigarettes. ATF investigation indicated this individual was dealing with customers in New York City. New York agents were able to identify 14 retail stores that probably would be selling contraband cigarettes. As a result, 6 arrests were made and 976.8 cartons of cigarettes with counterfeit stamps were seized.

#### Alcohol enforcement

In fiscal 1980, this program directed ATF resources toward the apprehension of persons who traffic in illicit alcohol, or violate Federal laws regarding regulations of the legal alcohol industry.

*Legal alcohol.*—In fiscal 1980, 31 investigations involving the legal alcohol industry were opened and 26 investigations were closed. These investigations include attempts by criminals to infiltrate the legal alcohol industry, falsification of records by regulated industry members, and other violations of the Federal Alcohol Administration Act.

*Illegal alcohol.*—ATF's efforts to protect the public safety and tax revenue have eliminated production and sales of illicit alcohol in many areas of the country. The volume of illicit liquor has been reduced in the remaining areas to a level where, in most instances, State and local authorities can control it effectively. This result has allowed ATF to investigate those liquor cases where geographic and jurisdictional constraints, or possible conspiracy, precluded successful State or local enforcement. In fiscal 1980, a total of 44 illegal stills, 9,045 gallons of mash, and 869 gallons of nontaxpaid distilled spirits were seized.

A task force was assigned to investigate and perfect criminal cases against some of the larger illicit whiskey violators in Franklin County, Va. With the assistance of Virginia Alcoholic Beverage Control agents, this investigation resulted in 2 conspiracy cases and 11 substantive cases involving 21 persons, and the seizure of 6 distilleries consisting of 60 stills having a utilized mash capacity of 47,400 gallons. If these stills had remained operational for 1 year, they would represent an estimated tax evasion to the Federal Government of over \$3.5 million.



### Miscellaneous enforcement activities

In fiscal 1980, ATF developed a strategy which allowed each district office to conduct a crime assessment in its geographic area of responsibility. Since the crime problem varies greatly from area to area, this strategy will allow ATF to determine how criminal enforcement resources should be best applied and will afford greater latitude to each level of management for combating crime in its particular area.

A staffing model for the criminal enforcement field offices has become operational. It correlates field agents with identified violations within ATF's enforcement responsibilities. This procedure is expected to increase the quality and quantity of individual agent productivity.

A management assessment center to develop and select first-level field supervisors became operational in fiscal 1980. ATF is developing a similar approach, known as MAC-II, for midlevel management positions.

ATF processed an estimated 2,700 "relief from disability" applications in fiscal 1980. Applications were based on requests by persons prohibited from owning firearms because of felony convictions.

During fiscal 1980, ATF special agents provided assistance to the Secret Service for the Presidential campaign.

## Regulatory Enforcement

### Compliance

To ensure the determination and collection of more than \$5.6 billion in alcohol excise taxes, 5,548 revenue protection inspections were conducted at distilleries, breweries, and wineries. Inspectors conducted 4,298 application and 1,969 consumer protection inspections. ATF accepted 32 offers-in-compromise totaling \$2.6 million from alcohol industry members for violations of Federal alcohol and tax laws. ATF continued with implementing the Distilled Spirits Tax Revision Act of 1979 which simplified the determination and collection of distilled spirits taxes. The newly established Regulatory Audit Staff began a review of all distilled spirits plants' internal control. All registered distilled spirits plants must have certification approval of their internal recordkeeping system, ensuring proper determination and payment of alcohol excise taxes, before ATF personnel can be withdrawn from the premises. As of August 1980, 2 distilled spirits plants had received approval, while 36 additional plants were under review.

### Alcohol regulations

*Gasohol.*—With the passage of the Crude Oil Windfall Profit Tax Act of 1980 (Public Law 96-223), ATF regulations have been implemented rapidly. Over 800 applications for alcohol fuel permits were received, 474 were approved, and the remainder were withdrawn or abandoned by the applicants in 1980.

As a result of widespread interest in alcohol fuel, ATF proposed statutory revisions which reduced the requirements for qualification and operation of facilities producing alcohol intended for fuel use. Those proposed revisions were included in the Crude Oil Windfall Profit Tax Act and became effective July 1, 1980. New ATF requirements for alcohol fuel producers have been simplified, particularly for small and medium volume producers. Previously approved experimental still permits numbering 4,428 have been converted to alcohol fuel permits, with many more under consideration.



State and public conferences and a series of congressional seminars were held to inform both the public and government officials on the regulatory requirements for alcohol fuel permits.

*Advertising regulations.*—ATF is sponsoring regulations concerning the advertising of wine, distilled spirits, and malt beverages (beer, ale, stout, etc.). These proposed regulations will introduce new regulations, update current regulations, and incorporate old rulings and circulars into the regulations. The Bureau believes these proposed regulations will allow freer competition among members of the alcoholic beverage industries, provide a single source of rules and regulations regarding advertising, and protect consumers from false or misleading advertising.

*Viticultural areas.*—In June 1980, ATF established the first American viticultural area, "Augusta," in Missouri. Several petitions from New York, California, and other States are pending. Viticultural areas are grape-growing regions which have boundaries based on geographic factors such as soil, rainfall, and temperature. The name of an approved viticultural area may be cited on labels and in advertising as a wine's appellation or place of origin.

*Ingredient labeling.*—The final ATF regulations governing partial ingredient labeling requirements were published in the Federal Register on June 13, 1980.

*Fetal alcohol syndrome.*—ATF is continuing to monitor the public education program to determine whether or not it will be necessary to consider fetal alcohol syndrome warning labels on alcoholic beverages. ATF has been working with the Department of Health and Human Services to prepare a report to Congress on ways to alert the public to health hazards connected with alcohol.

*Voluntary disclosure.*—Since 1976, ATF has encouraged persons and businesses subject to ATF jurisdiction to disclose, voluntarily, suspected violations of laws and regulations administered by the Bureau. It has been made clear that such disclosure will be viewed as a mitigating factor in reaching decisions to restore compliance; however, voluntary disclosure would not result in immunity from criminal, civil, or administrative action. Several major companies made disclosures and have been or are being investigated. Voluntary disclosure investigations closed this year resulted in four offers-in-compromise. Over a dozen investigations are either continuing or pending final action.

*Nationwide investigations.*—Nationwide investigations of major industry members believed to have committed illegal marketing practices are continuing. These are not industry members who have reported questionable trade practices under ATF's ongoing voluntary disclosure policy.

#### Firearms regulations

Seminars continued to be held on firearms laws and regulations throughout the country as part of ATF's regulatory information program. An exhibit describing ATF's regulatory role appeared at conventions and shows throughout the country with ATF officials on hand to answer questions from the public.

#### Explosives program

ATF has begun preparation for a presentation to Mine Safety and Health Administration (MSHA) inspectors on ATF explosives storage and record-keeping requirements. This is a result of a cooperative agreement signed by ATF and MSHA concerning explosives safety regulations at mining sites.

### Tobacco program

The Bureau processed 400 claims for tobacco tax refunds and conducted 634 revenue protection inspections and 83 application inspections to ensure the collection of just under \$2.5 billion in Federal revenue.

Regulatory enforcement is providing assistance, upon request, to State governments and ATF criminal enforcement in investigations concerning Public Law 95-575, prohibiting the possession and transportation of contraband cigarettes. ATF regulations governing contraband cigarettes have been finalized and were put into effect on September 19, 1979.

## Technical and Scientific Services

### Laboratory system

The laboratory system is comprised of the National Laboratory Center and four field laboratories serving regional areas of the United States. The laboratories provide ATF with a comprehensive scientific capability for the support of regulatory and criminal enforcement activities.

In the regulatory area, more than 32,000 items were examined to protect consumers and to validate excise tax collections. A growing concern on consumer matters has resulted in the laboratory system performing more tests. The verification of caloric and nutritional claims on light beers, the detection of artificial colors or flavors, and the monitoring for the presence of restricted or prohibited ingredients constitute a significant part of the current activities in the laboratory system. Special areas of investigation include a fermentation study of tobaccos for tax classification and development of a digital density meter to improve the method of proofing alcoholic products. The laboratory has also been actively involved in the development of improved denaturant formulations for use in the manufacture of ethyl alcohol in gasohol applications.

The field laboratories and the Forensic Science Branch at the National Laboratory Center conducted 12,277 firearms examinations, 18,300 explosives examinations, and 425 counterfeit cigarette tax indicia examinations. These examinations included such support examinations as fingerprint, document, ink, paper, voiceprint, tape processing, toolmarks, and a large variety of trace evidence analyses.

The Forensic Science Branch implemented a new training program to train State and local arson chemists on laboratory methods for the detection and identification of accelerants in arson debris. A total of 51 chemists representing over 30 States were trained. Forensic personnel also participated in numerous LEAA-ATF arson-for-profit and cigarette smuggling sessions given throughout the United States for State and local investigators.

A major research breakthrough was made in the field of ink dating which represents the single greatest accomplishment in this field since the implementation of the ink program in the Forensic Science Branch in 1968. A technique was developed to measure the relative age of inks on questioned documents. This technique is now being applied routinely to questioned documents related to arson, firearms, and explosives examinations.

### Technical services

Firearms enforcement officers and analysts supported more than 300 Federal crime investigations during fiscal 1980. Approximately 600 firearms, silencers, and destructive devices were tested. Courses of instruction were presented to State and local law enforcement agencies under an LEAA

program, and assistance was provided to manufacturers and importers in classifying and marking newly designed firearms.

The National Firearms Tracing Center conducted about 40,000 firearms traces in fiscal 1980. Firearms were traced to the point of the first retail sale to assist Federal, State, and local law enforcement agencies. Special trace studies were conducted in selected cities in an effort to determine the origin and flow of firearms used in crimes throughout the United States.

ATF acted on more than 16,000 applications involving the manufacture, transfer, importation, and exportation of over 172,000 National Firearms Act (NFA) weapons. These were controlled weapons which include machine-guns, short-barreled shotguns, short-barreled rifles, and silencers. Approximately 1,200 evidence certifications were prepared for recovered NFA weapons not recorded, as required by law, in the National Firearms Registration and Transfer Record.

In fiscal 1980, the ATF Imports Branch processed over 15,000 import permit applications. A total of 824,110 firearms and 92 million rounds of ammunition were reported as having been imported into the United States.

ATF gave assistance in 2,800 explosives incidents. This included onsite investigative aid, determinations relating to explosives and destructive devices, explosives tracing, furnishing court testimony, and the destruction of explosives and other hazardous materials.

#### Data processing

The criminal automated reporting system was extensively modified to include reporting for enforcement priority tracking.

The certificate of label approval system was implemented with an approximate \$35,000 savings to ATF per year.

Two new automated systems, the personnel automated staffing system and the regulatory information management system, came online, providing management information regarding personnel and program source utilization.

### Administration

#### Financial management

The Bureau's operating budget for fiscal 1980 was \$142 million. Approximately 73 percent of this amount was spent on salaries and benefits for ATF's employees. The remainder was allotted to communications and office space (9 percent); official travel (4 percent); printing (2 percent); and miscellaneous items and specialized equipment (12 percent).

#### Personnel management

One of ATF's primary administrative tasks during fiscal 1980 was to prepare for full implementation of the Civil Service Reform Act (CSRA). Three initiatives were completed during the year. First, ATF's executive development program was redesigned to provide enhanced management training opportunities for present and potential managers in the Senior Executive Service. Second, all managerial and supervisory positions in grades 13 through 15 were identified for inclusion in the merit pay system, which will be implemented on March 1, 1981. Finally, all ATF management personnel were trained in the development of performance standards for positions under their supervision. As required by law, all of the changes specified in the CSRA will be in place by October 1981.



### Communications

As a part of its continuing support of ATF field personnel, the ATF Communications Center processed 700,000 messages in fiscal 1980. These transmissions assisted special agents in locating 261 fugitives and 85 stolen firearms. In addition, plans were made to install a secure teletype network between headquarters and the principal field offices. The proposed network would permit field sites to assist other Treasury agencies requiring secure transmission facilities.

### Training

During fiscal 1980, more than half of ATF's employees attended professional development courses. Approximately two-thirds of all training was in technical specialties related to law enforcement or regulatory activities. Senior managers, supervisors, and support personnel attended courses in the management, administrative, legal, and scientific areas. ATF also provided 27 LEAA-funded training sessions for approximately 1,000 State and local law enforcement personnel. These sessions taught investigative techniques used in arson-for-profit and cigarette-smuggling cases, firearms identification, and the detection and identification of accelerants found in arson debris.

### Paperwork management

Efforts to reduce the reporting burden of the regulated industries continued in fiscal 1980. Twenty-eight forms were eliminated, and 139 others were shortened or revised. Sixty of these actions were related to implementation of the Distilled Spirits Tax Revision Act of 1979. Seven monthly reports previously required from winemakers also were abolished.

### Printing

The Bureau of Engraving and Printing reduced its charge for printing alcoholic beverage strip stamps by approximately 35 percent. As a result, ATF realized a savings of \$250,000 during fiscal 1980.

### Out-of-business firearms dealer records

Since 1975, ATF has accumulated records from over 45,000 out-of-business firearms dealers at its storage facility in Arlington, Va. In fiscal 1980, the REMAC Corp. began microfilming these documents under a contract with ATF. When the project is completed, ATF expects to trace lost or stolen firearms more efficiently, and to reduce significantly its document storage requirements.

### Energy conservation

During fiscal 1980, ATF placed a high priority on conserving energy in daily operations. As a result, the overall gasoline consumption of ATF vehicles was 9 percent lower than in fiscal 1979.

## Research and Development

In fiscal 1980, significant progress was achieved in the development of an explosives tagging capability designed to reduce the number of criminal and terrorist bombings. Developments in explosives tagging were aimed at providing law enforcement and security personnel with modern technological tools to detect explosives before they detonate (detection tagging) and to



identify and trace explosives used in bombs after they detonate (identification tagging).

#### Explosives tagging for identification

Identification tagging to help solve bombing crimes is well on the road to achievement. The basic research and scientific aspects could possibly be completed in fiscal 1981. The report on tagging issued by the Office of Technology Assessment in April 1980 found that " \* \* \* the testing done to date creates a reasonable presumption that the 3M identification taggant is compatible with dynamite, gels, slurries, emulsions, and black powder."

Ongoing tests demonstrated taggant survivability and recoverability in all tested explosives. The feasibility of tagging detonating cord and safety fuse was established, and a simulated taggant applicator for use in manufacturing detonating cord was constructed. The identification tagging of blasting caps is a complex problem and technical development is not yet complete.

ATF testing indicated that further research is also required on at least one smokeless powder brand and one cast booster material as the result of a chemical reactivity with identification taggants under severe overtest conditions. However, this reactivity occurs only with one manufacturer's brand of smokeless powder and one cast booster type. It does not appear in all powders and boosters nor in other explosive materials.

Additional tests were contracted with independent laboratories to determine the cause and extent of the chemical reactivity in the one powder and the booster material. The results of these tests will determine what action is required to insure that tagging of explosives does not compromise the safety of these products.

Evidence of the usefulness of identification tagging was demonstrated in a recent Baltimore, Md., fatal bombing. The explosives used in the bombing/murder had been tagged under an ATF test program and sold through normal commerce. The taggants enabled ATF agents to trace the purchase of the explosives to the victim's uncle. The suspect was found guilty of the crime and in April 1980 was sentenced to 30 years in prison. The U.S. attorney handling the case formally stated in a letter to ATF that " \* \* \* the investigation and prosecution succeeded largely because of the discovery of taggants at the crime scene."

#### Explosives tagging for detection

Development of a detection taggant and taggant vapor detection instruments to signal the presence of a bomb before it explodes progressed significantly in fiscal 1980.

A single vapor chemical was selected from hundreds of potential candidates as the optimum vapor for use in the detection taggant. Research with three possible systems for encapsulating the taggant vapor to allow a continuous rate of vapor release for a 5-year period was begun.

Four vapor taggant detection systems were developed: (1) An ion mobility spectrometer, (2) a continuous electron capture detector, (3) a mass spectrometer, and (4) use of animals. All systems were completed to the feasibility stage, and a decision will be made in early fiscal 1981 to concentrate efforts on developing the most promising detection system.

#### Untagged explosives detection

While detection tagging is expected to provide a substantial deterrent effect, the development of untagged explosives detection methods remained a

major priority. In fiscal 1980, designs for a promising dual-energy computerized tomographic explosives detection system were developed, and completion of a breadboard unit is scheduled for early fiscal 1981.

### Planning and Evaluation

The Office of Planning and Evaluation was established on January 31, 1980. It is headed by an Assistant Director and has two divisions: Program Planning and Operations Research and Evaluation.

The office is responsible for developing and implementing a strategic planning process. The process includes an incremental implementation to begin in fiscal 1981 with publication of a situation report or environmental assessment, identification of planning units, and publication of a multiyear strategic plan and definitive operational plans.

The office is also responsible for a major portion of evaluation efforts for ATF. This includes development of plans for evaluation projects, incorporating evaluation into the strategic planning process, and working with other offices to develop their own evaluation capabilities. Evaluation efforts in fiscal 1980 focused on applying statistical methodologies to specific programs.

### Chief Counsel

Chief Counsel worked with ATF officials in the development of numerous major rulemaking projects including the drafting of temporary regulations under the Distilled Spirits Tax Revision Act of 1979, the alcohol for fuels legislation, final ingredient-labeling regulations, proposed new trade practice and advertising regulations under the Federal Alcohol Administration Act, and implementing regulations under the new trafficking in contraband cigarettes law.

Counsel worked closely with ATF officials in the development of ATF's firearms, arson, and contraband cigarettes programs, and in the preparation of testimony before congressional committees.

ATF attorneys also provided training to ATF employees in the areas of legal rights and responsibilities of ATF inspectors and auditors, disclosure laws, and personnel matters.

Staff attorneys represented ATF in administrative hearings, prepared litigation reports and appeal recommendations, and assisted the Justice Department in the preparation of briefs. Counsel has been actively involved in all significant litigation concerning ATF, particularly recent cases involving Federal authority under the 21st amendment of the Constitution. In *G. William Miller v. Castlewood* the Supreme Court vacated and remanded a decision by the Fifth Circuit which would have restricted Federal authority over intoxicating liquor under the 21st amendment in favor of State law. The Fifth Circuit is currently reconsidering the case. In another case, *Goldstein v. Miller*, involving Federal primacy in the area of intoxicating liquor, the Government won a significant victory. In that case the U.S. District Court for Maryland held that the 21st amendment did not prevent the Federal Government from establishing an exclusive list of liquor bottle sizes which did not include a size permitted by the State of Maryland.

### Public Affairs and Disclosure

News releases, factsheets, special feature articles, speeches, brochures, and public service radio spots were released to the public, news media, law

enforcement community, regulated industries, and other Government agencies concerning ATF's mission.

Public awareness programs on arson and cigarette smuggling were initiated to educate the public through the news media.

ATF's public awareness campaign to educate the public about the relationship between alcohol consumption by pregnant women and birth defects moved ahead. The first 750,000 copies of a publication on this syndrome, featuring the character of Rex Morgan, M.D., were distributed with the assistance of many government agencies, industry, medical, educational, and public service organizations.

Nine hundred copies of a short television spot announcement entitled "Two Tummies" have been sent to the television networks and local TV stations.

A formal speakers bureau was formed and will be conducted through ATF field offices in the 50 States.

The Disclosure Branch responded to a 15-percent increase in Freedom of Information Act requests and a 30-percent increase in Privacy Act requests during fiscal 1980.

Freedom of Information Act requests numbered 753, of which 542 requests were granted in full, 181 were granted in part, and 30 were denied. Of 10 administrative appeals, 1 was granted in full, 2 were granted in part, and 4 were denied. Three appeals are still being processed. Fees collected for Freedom of Information Act requests totaled \$5,256.

Privacy Act requests numbered 703, of which 696 were initial requests for access to records; 2 were requests to amend records and 5 were requests for an administrative appeal to the Director. Eighty-five percent of the initial requests were granted—447 in full, 150 in part. Five percent of the requests were denied.

A primary purpose of the Privacy Act is to assure accuracy in the collection of data about individuals. Both requests to amend records were granted. Statistics indicated 98.9 percent of all requesters granted access to their records did not question the accuracy of such records.

Field employees were trained in disclosure practices during the year. Refresher training and course instruction was expanded for new agents and inspectors.

### **Congressional Affairs**

The Office of Congressional Affairs is responsive to congressional inquiries concerning the programs and regulations that ATF implements. ATF responded to numerous written and telephone congressional inquiries. In addition, testimony was prepared for presentation at congressional hearings, and seminars were held on issues of special interest to congressional offices.

### **Equal Employment Opportunity**

ATF equal opportunity programs include affirmative action, which encompasses recruitment and community outreach; Federal women's and Hispanic employment special emphasis areas; and upward mobility.

To carry out these responsibilities, ATF promotes activities necessary for the acceptance and enhancement of the total equal opportunity program within ATF. The ATF Director has actively sought to improve the representation of minorities and women in ATF, as well as encouraged management officials to be aggressive in their plans for an active program.



As part of the equal opportunity effort, ATF is committed to advance minorities and women into mid- and upper-level positions.

During the year, the Assistant to the Director (EO) visited each ATF region. The equal opportunity program was reviewed, and each manager was briefed on the role he or she must play to assure that equal opportunity considerations become an integral part of the Bureau and its mission.

Programs in the Bureau are producing results that have improved hiring and promotion of minorities and women. Women currently represent 32 percent of the Bureau's employees, other minorities almost 11 percent. Women now hold 230 of 938 positions in the 1854/regulatory inspector series. Blacks and other minorities hold 29 percent of these positions. In the 1811/special agent series, 114 of 1,601 total special agents are women and minorities.

### Internal Affairs

The Office of Internal Affairs was reorganized in fiscal 1980, resulting in the decentralization of the investigations function. Regional offices have been established in Atlanta, New York, Chicago, and San Francisco with satellite offices in Cincinnati and Dallas.

Internal audits conducted in fiscal 1980 resulted in 42 recommendations which provided an independent evaluation of ATF operations, identified savings and cost-avoidance opportunities of approximately \$1 million, questioned costs of \$381,500, and led to improvements in ATF programs.

A total of 259 integrity investigations were initiated during the fiscal year; 142 were completed and resulted in 5 resignations, 28 adverse actions, and 3 referrals to other law enforcement agencies. The remaining 106 investigations disclosed no misconduct.

New employee background investigations and security updates totaled 698. In fiscal 1980, 437 security investigations and/or updates were completed and 261 were underway at the end of the fiscal year.

## OFFICE OF THE COMPTROLLER OF THE CURRENCY<sup>1</sup>

The Office of the Comptroller of the Currency (OCC) was established in 1863 by the National Currency Act, redesignated in 1864 as the National Bank Act (12 U.S.C. 38). As Administrator of National Banks, the Comptroller is charged with regulating and supervising the national banking system, within existing statutes and in a manner which best serves the public interest. During fiscal 1980, the effects of inflation, monetary policy, declining U.S. economic growth, and sharply higher energy costs induced many changes within the financial system. Critically, there was a large increase in the demand for financial instruments with competitive market yields such as money market certificates of deposit and money market mutual funds.

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<sup>1</sup> Additional information is contained in the separate Annual Report of the Comptroller of the Currency.



The total assets of the national banking system, both foreign and domestic, grew by 11.7 percent in 1979 to \$996.3 billion; this rate was slightly below the 12-percent growth of 1978. The total number of national banks declined for the fourth consecutive year. At yearend 1979, there were 4,448 national banks, 116 fewer than 1978.

#### Bank examinations

Bank examination is among OCC's principal tools for carrying out its responsibility to promote and ensure the safety and soundness of the national banking system. Examinations provide an objective evaluation of a bank's soundness, appraise the quality of management, and identify areas requiring corrective action. In 1979, OCC employed 2,282 examiners and performed 3,998 commercial examinations, 1,245 trust examinations, and 863 electronic data processing examinations.

During 1979, efforts were made to improve the efficiency of the examination function by adapting the scope of an examination to an institution's size and/or condition. Specialized and small bank trust examinations and specialized electronic data processing examination procedures were developed.

Supervision of the 11 largest national banks and other national banks with significant international activities is vested in OCC's Multinational Banking Division. At the end of 1979, those banks held 42 percent of the national bank assets and 25 percent of the entire U.S. banking system assets. The Multinational Banking Division is responsible for the examination process, financial analysis, corporate activity, and all phases of supervision. In 1979, as an extension of the examination process, OCC began a quarterly visitation program for multinational banks. The goal is to obtain more frequent and timely information on the financial condition, activities, and plans of those institutions.

#### Banking organization and structure

OCC is required by statute to pass upon certain structural changes in the commercial banking system. Among these actions are: Applications for new banks, branches, relocations, title changes, Federal branches and agencies of foreign banks, mergers, and consolidations. In addition to processing requests, OCC is responsible for maintaining structure records such as title, location, number of offices, and amount of capital stock of each national bank.

Although there was a significant increase in volume of applications during 1979, considerable progress was made in reducing processing time, improving the quality of corporate analysis, and reducing the regulatory burdens on the industry. Charter application processing time decreased from 134 to 63 days. Also, procedures were adopted to process expeditiously certain applications at the regional office level, eliminating duplicative review in Washington.

#### Banking research and economic programs

OCC conducts a broad range of research programs and studies on issues of current and potential importance to its bank regulatory and supervisory responsibilities. It also monitors developments in the financial services industry and evaluates their impact on the banking system and OCC's operations. In June 1980, OCC released a series of 14 staff papers that resulted from a comprehensive review of foreign acquisitions of U.S. banks. The papers not only compile basic factual information but also consider the

implications of such acquisitions for banking competition and the performance and supervision of banks.

Based on information derived from its research on housing-related lending, OCC proposed rules governing the use of adjustable-rate mortgages by national banks.

#### Customer and community programs

OCC is responsible for the enforcement of numerous consumer protection statutes as they relate to the activities of national banks. This responsibility is fulfilled by various actions of the Office, including consumer examinations, complaint resolution, and educational programming.

During 1979, OCC conducted 2,249 consumer examinations of national banks. Also, 12,650 consumer complaints were received, representing a 12-percent increase over 1978. That increase was considerably smaller than in previous years. The average complaint resolution time has consistently decreased over the past 3 years.

OCC created the position of Special Assistant for Civil Rights in 1979 to oversee OCC efforts to comply with the fair housing suit settlement agreement with the National Urban League, advise OCC divisions on civil rights matters, initiate programs and policy changes to strengthen responsiveness to civil rights issues, and act as liaison with civil rights groups. In 1979, the Special Assistant's primary task was the development and implementation of the fair housing home loan data system regulation.

The Community Reinvestment Act (CRA) requires that OCC assess each bank's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, to consider that record in any evaluation of an application for a deposit facility, and to encourage banks to help meet the credit needs of their communities. In early 1979, OCC and the other Federal financial regulatory agencies adopted a preliminary CRA bank performance rating system. OCC also sought ways to help educate bankers and the public about CRA. The agency held a series of workshops in which representatives from civil rights, consumer, community, and banking groups were brought together to discuss CRA-related issues.

#### Regulations analysis

OCC conducts a continuing review of its regulatory program to identify and eliminate unnecessary regulatory burdens through careful analysis of existing and newly proposed regulations.

During this period, OCC revised 20 regulations and 12 interpretive rulings. These revisions permitted the removal of more than 200 pages from the Code of Federal Regulations containing specific investment security rulings, a reduction in recordkeeping requirements for banks conducting securities transactions, and more expeditious processing by national banks of their securities offerings to the public without compromising the needs of investors.

#### Chief Counsel

The Chief Counsel advises the Comptroller on legal matters arising in administration of laws, rulings, and regulations governing national banks, as well as participating in litigation involving OCC and exercising certain direct responsibility in enforcement and securities matters. Attorneys deal directly with the management of national banks, with bank attorneys and accountants,

and with the staffs of other Government agencies and congressional committees.

At the beginning of 1979, 79 lawsuits were pending. The OCC paralegal unit received 4,498 new consumer inquiries. Also, the unit resolved 1,042 complaints. The number of formal administrative actions under the Financial Institutions Supervisory Act increased approximately 21 percent over the preceding year to reach 93.

#### Operations

The Senior Deputy Comptroller for Operations is responsible for the overall operational effectiveness and efficiency of OCC. He supervises the 14 regional offices, Management Services, Finance and Planning, Systems and Data Processing, Human Resources, and Equal Employment Opportunity.

Major project activities for the Systems and Data Processing Division included operation of OCC's national bank surveillance system and the production of quarterly bank performance reports for all national banks, all Federal Reserve member banks, and all State banks in New York, Virginia, and Nevada. Development of the national bank surveillance display system will eventually allow bank examiners to acquire critical national bank data on demand.

The Deputy Comptroller for Administration and the EEO Officer under the Human Resources Division developed population-based hiring goals, a computerized recruitment resources information system, an advertising campaign directed at minority and female media, and other EEO programs.

## OFFICE OF COMPUTER SCIENCE

The Office of Computer Science furnishes computer and related support for the analytical, policy formulation, accounting, and administrative functions of the Office of the Secretary and the bureaus. The Office also assists in computer development work for Treasury bureaus which do not have their own facilities. It provides Department-wide, centralized management review, approval, and guidance for ADP management planning, policy, and evaluation activities.

The Computer Center, operated by the Office of Computer Science, has a Univac 1100/81 computer system to serve its customers. The Center now serves 60 organizations concentrating on econometric analyses and administrative processing.

During fiscal 1980, a contract was let with Sperry Univac to upgrade the present computer system. The new system will be installed in the vault area of Main Treasury and will meet most of the Office of the Secretary computer mainframe requirements through fiscal 1986. Additional competitive procurements are underway to replace the remote job-entry stations and to provide supplementary local processing capability.

The accounting portion of the financial system for the Financial Management Division was successfully automated in fiscal 1981. This is a fully integrated financial system which includes both obligation and general ledger accounting for current and prior fiscal year. The budget module for future fiscal years is planned for implementation next year. These systems provide



support for Office of the Secretary salaries and expenses, Office of Revenue Sharing funds, the Office of the Secretary working capital fund, New York City fund, Chrysler Corp. fund, and the International Affairs fund.

One of the larger undertakings underway is automation of the loan activity of the Federal Financing Bank.

## OFFICE OF DIRECTOR OF PRACTICE

The Office of Director of Practice is part of the Office of the Secretary of the Treasury and is under the immediate supervision of the General Counsel. Pursuant to the provisions of 31 CFR, part 10 (Treasury Department Circular No. 230) and the provisions of 31 CFR, part 8, the Director of Practice institutes and provides for the conduct of disciplinary proceedings against attorneys, certified public accountants, enrolled agents, and other individuals who are alleged to have violated the rules and regulations governing practice before the Internal Revenue Service or the Bureau of Alcohol, Tobacco and Firearms. He also acts on appeals from decisions of the Commissioner of Internal Revenue denying applications for enrollment to practice before the IRS made under 31 CFR, section 10.4, and appeals from decisions of the Director, Bureau of Alcohol, Tobacco and Firearms denying applications for enrollment to practice before ATF made under 31 CFR, section 8.21. In addition, the Director of Practice serves as Executive Director of the Joint Board for the Enrollment of Actuaries. The Joint Board, formed pursuant to section 3041 of the Employee Retirement Income Security Act of 1974 (ERISA), is responsible for the enrollment of individuals who wish to perform actuarial services under ERISA and for the conduct of disciplinary proceedings against enrolled actuaries who are alleged to have violated the rules and regulations governing the performance of those services.

During fiscal 1980, regulations were promulgated to implement the application of title V of the Ethics in Government Act of 1978 addressing postemployment conflicts of interest by former officers and employees of the Department of the Treasury. The regulations established that the Director of Practice shall institute and provide for the conduct of disciplinary proceedings involving former employees of the Department. The final rule, published as part 15 to title 31 CFR, appeared in 45 F.R. 115, dated June 12, 1980. In addition, amendments to the provisions of Circular 230 were proposed to include standards for the providing of opinions used in the promotion of tax shelters.

Notice of the proposed rule appeared in 45 F.R. 173, dated September 4, 1980. Publication of the final rule on the proposal was pending at the end of the fiscal year.

On October 1, 1979, there were 157 derogatory information cases pending in the Office under active review and evaluation, 16 of which were awaiting presentation to or decision by an administrative law judge. During the fiscal year, 107 cases were added to the case inventory of the Office. Disciplinary actions were taken in 58 cases by the Office or by order of an administrative law judge. Those actions were comprised of 11 orders of disbarment, 31 suspensions (either by order of an administrative law judge or consent of the practitioner), 1 resignation, and 15 reprimands. The actions affected 16



attorneys, 29 certified public accountants, and 13 enrolled agents. Thirty-eight cases were removed from the Office case inventory after review and evaluation showed that the bases of allegations of misconduct would not support disciplinary proceedings under 31 CFR, part 10 or under 31 CFR, part 8. As of September 30, 1980, there were 168 active cases in the Office.

During the fiscal year, 12 attorneys, certified public accountants, and enrolled agents under suspension or disbarment from practice before the IRS petitioned the Director of Practice for reinstatement of their eligibility to resume practice. Favorable disposition was made on 10 of those petitions and reinstatement was granted. One petition was denied. One petition was pending at the close of the fiscal year. In addition, the Director of Practice granted a petition pending from fiscal 1979. There was one appeal from denial by the Commissioner of Internal Revenue of an application for enrollment to practice before the IRS during the fiscal year. The appeal remained pending at the year's end.

Twenty-four administrative proceedings for disbarment or suspension were initiated against practitioners before the IRS during fiscal 1980. Together with the 16 cases remaining on the administrative law judge docket on October 1, 1979, 40 cases were before the administrative law judge during the year. Nine of those cases resulted in the acceptance of an offer of consent to voluntary suspension from practice before the IRS pursuant to 31 CFR, section 10.55(b) prior to the conclusion of proceedings. Initial decisions imposing disbarment were rendered in 15 of the cases, and an initial decision imposing suspension was rendered in 1 case. One complaint was withdrawn. On September 30, 1980, 14 cases were pending on the docket awaiting presentation to or decision by an administrative law judge.

During fiscal 1980, six cases were appealed to the Secretary from initial decisions of the administrative law judge. One case resulted in an affirmation of the order of disbarment and one case resulted in an affirmation of the order of suspension. The remaining four appeals were pending at the year's close. In addition, two decisions were issued on appeals pending on October 1, 1979. In both instances, the administrative law judge's initial decisions of disbarment were affirmed.

Twenty-one meetings of the Joint Board for the Enrollment of Actuaries were held during the fiscal year. On October 1, 1979, there were 90 applications pending under the regulations governing enrollment, and 149 applications were filed during the year. Of these, 172 applicants were enrolled, 6 applicants were denied enrollment, and 7 withdrew. Fifty-four applications were pending at the close of the fiscal year.

During the fiscal year, there were 33 derogatory information cases before the Joint Board. After review and evaluation of the cases, the Executive Director issued reprimands to three enrolled actuaries. Seven cases were removed from the case inventory after evaluation showed that the bases of allegations of misconduct would not support disciplinary proceedings. Twenty-three cases were pending at the close of the fiscal year.

To assist the Joint Board in the performance of its examination duties, the Joint Board Advisory Committee on Actuarial Examinations met eight times during the fiscal year. The Joint Board administered three qualifying actuarial examinations during fiscal 1980. The examinations were administered jointly with three private actuarial organizations.

## BUREAU OF ENGRAVING AND PRINTING

The Bureau of Engraving and Printing is the world's largest securities manufacturing establishment. It designs and produces U.S. currency, postage stamps, public debt securities, and other, miscellaneous financial and security documents issued by the United States.

### Finances

The operations of the Bureau of Engraving and Printing have been financed since July 1, 1951, by means of a revolving fund established by Public Law 656, August 4, 1950 (31 U.S.C. 181), as amended by Public Law 95-81, July 31, 1977. The amendment authorized the Bureau to include in the charge for its products (in addition to cost of manufacturing and services performed) an amount to be accumulated for the procurement of capital equipment and to provide for future working capital. Agencies which the Bureau serves are required to make reimbursement for all costs incidental to the performance of work or services requisitioned.

Congress has supplied appropriations as increases to the fund on three occasions since the inception of the revolving fund. The appropriated portion of the revolving fund is \$14,250,000. The Bureau financed a program at a total cost of \$111,256,151 in fiscal 1980, as compared with \$132,109,381 in fiscal 1979 by means of this fund.

Bureau operations during fiscal 1980 resulted in accumulated retained earnings of \$11,140,175.

The Office of Financial Management has a number of self-contained but related automated and manual financial information subsystems. They have resulted in a heavily labor-intensive operation which often requires duplicate data entry to various systems and requisite manual reconciliation between subsystems. These deficiencies cause delays in monthend financial closings, inaccuracies in production costs, and inability to provide management with timely financial information. To alleviate these problems, Bureau management determined that a new, automated financial management information system should be developed. When completed, this system will result in substantial savings through increased efficiency and staff reductions. Target date for completion of this project is fiscal 1983.

The Bureau established a task force responsible for developing, designing, and implementing the system. During fiscal 1980, the task force developed a solicitation engaging the services of a design contractor to perform a requirements analysis and to develop a conceptual design for the system. This initial contract was awarded during September 1980; it is anticipated that the duration of this initial contract will be 10 to 12 months.

During fiscal 1980, the Director implemented a management information and control system for the Bureau. This system encompasses a resource management concept which allows designated managers to participate more fully in the operations of the Bureau and presents them with new and more challenging management responsibilities.

Bureau managers are now accountable for both the quality and costs of the services they provide. Each significant Bureau resource is made the responsibility of a designated manager, who is required to ensure that the resource supports the planned Bureau goal during the fiscal year. This is accomplished by preparing a written plan which indicates subsidiary goals for the year with clear delineation of the plan to meet these goals. Periodically each manager is required to present actual program progress to all other

Bureau managers, comparing actual results with planned action. This serves to keep all managers aware of significant events that may impact their areas.

The resource management system has enabled the Bureau to improve manager accountability, reduce the level of decisionmaking, and develop many supervisors into managers. In fiscal 1980, despite a 10- to 13-percent inflation rate, the Bureau was able to execute its mission at the same cost level as the prior year. As a result of the management information and control system, Bureau operating costs were reduced approximately \$10 million.

#### Currency program

Deliveries of currency in fiscal 1980 totaled about 3.6 billion notes, as compared with about 3.8 billion notes in fiscal 1979.

Two new currency presses, type Intaglio 8, utilizing water base inks, have been specified, ordered, and factory tested. Delivery and installation will begin on or about October 1, 1980. Currency overprinting equipment has also been specified and final contract negotiations are being completed. These acquisitions, coupled with the two optional intaglio presses, will increase the currency production capacity of the Bureau by approximately 28 percent when complete.

The development and implementation of updated quality standards have yielded an increase in the percentage of perfect work due to improved consistency during the inspection process. As a result of this program, the percentage of spoilage was reduced by 30 percent.

The development of a prototype automatic currency inspection system was completed at the factory during fiscal 1980. Long-term potential for this system appears to be substantial based on preliminary factory tests and inspections. The impact on currency inspection operations will be decisive when fully operative. Additionally, this equipment can provide for a highly sophisticated fault identification and diagnostic system for the immediate correction of defects. Estimated savings have not yet been determined. A special task force team is studying this and other impacts on operations and manpower requirements.

Analyses of a number of proposed major equipment acquisitions resulted in procurement of two items, based on noneconomic justifications, and procurement of three items economically justifiable. Modification of specifications related to two pieces of currency overprinting and processing equipment was recommended. It was anticipated that the changes would reduce the complexity of the equipment, result in a one-time cost avoidance of approximately \$1 million, and produce a recurring annual savings of approximately \$52,000.

#### Postage stamp program

In addition to regular postage stamp production, the Bureau processed and shipped 5.1 billion "special contingency stamps" (nondenominated) to U.S. Postal Service storage facilities. These stamps will be used in conjunction with a proposed postal rate increase scheduled for fiscal 1981. The Postage Processing Division delivered a total of 31.9 billion stamps to the U.S. Postal Service in fiscal 1980, as compared with 27.1 billion units in fiscal 1979.

Development activity regarding electronic machine counting of postage stamp sheets was completed during fiscal 1980. Immediate potential benefits of this improvement will abolish most manual counting. In the long term, the system will eventually reduce the total number of personnel required to process sheet stamps and result in a savings in excess of \$100,000 annually.



The nondenominated "B" issue was completed this year with a total of 5 billion stamps in books, sheets, and coils delivered to the U.S. Postal Service.

The 15-cent Dolly Madison issue was produced with 600 stamps per printed sheet to test the public's reaction to smaller postage stamps.

A study was conducted to evaluate the cost-effectiveness of alternative crew structures for the perforator-coilers. Use of a crew comprised of two craftsmen (bookbinders) was recommended, based on its cost reduction potential of \$155,000 annually. Production standards have been developed and this is expected to reduce operating costs annually by \$100,000.

Early study of postage stamp sheet production indicates a potential savings in the range of \$100,000 to \$150,000 annually when improved productivity methods are brought to completion. Similarly, improved productivity of the aerogramme processing is expected to yield annual savings of approximately \$19,000; and, in the sheet stamp splitting operation, improved productivity and reduced support staffing will produce recurring annual savings of \$31,000.

#### **Red strip stamps**

The Bureau discontinued the numbering of strip stamps as of March 31, 1980. This change in processing resulted in a decrease in the billing rate from \$0.75 to \$0.41 per 1,000 stamps.

#### **Production support activities**

Development of a production standard, determination of daily staffing needs, and establishment of a "labor pool" concept for covering absenteeism and miscellaneous tasks led to a decision to abolish 14 full-time custodial positions and eliminate weekend overtime by the use of part-time personnel. Savings exceeding \$25,000 annually are anticipated.

Fuel consumption in the Bureau has been reduced by 36 percent from fiscal 1979 usage. This accomplishment was achieved primarily by: (1) A Bureau-wide awareness program designed to inform managers and employees of the merits of a reduction in fuel consumption; (2) improved automotive trip scheduling and carpooling; and (3) contracting out some of the hauling activities associated with operational materials and supplies.

#### **Socioeconomic procurement accomplishments**

An extensive effort has been made to exceed the previously established total socioeconomic goal of \$6,750,000 out of estimated total fiscal 1980 procurement awards of approximately \$65 million. Through aggressive efforts, it appears that the Bureau will award a total in excess of \$7 million for the four identified categories in the socioeconomic programs. This is particularly significant in that this increase was accomplished even though total procurement awards during fiscal 1980 were some \$48 million, a substantial reduction from the estimated base.

#### **Ink and ink components**

Development of a new type of black paper-wipe currency ink, Bk-62 series, was accomplished during fiscal 1980. This ink formulation has been in almost exclusive use for currency production since early 1980. On-press working characteristics of this ink surpass those of the previously used Bk-60 series formulations. Modifications of this ink are continuing in order to optimize press runability.



Development of a press-acceptable water-wipeable green currency ink was also completed. Extensive press trials have shown that the most recent formulation meets all the press requirements for a successful production water-wipe printing ink. Quality assurance spoilage data collected during these trials indicate that this newly developed water-wipe ink formulation compares favorably with present paper-wipe ink spoilage data.

During the past year, extensive work was conducted toward the development of an improved tagging ink for U.S. postage stamps. These efforts have been directed toward improving the film integrity of the finished tag, and identifying phosphor materials that would have stronger and more efficient emission characteristics. While laboratory testing has shown that an experimental varnish system had significantly more film integrity towards abrasion than current production systems, incomplete results from Postal Service field tests show that the experimental varnish system does not have any appreciable advantages over the current production systems. Likewise, the newer phosphor materials evaluated show slight but no significant improvement in emission characteristics.

#### Forensic research and development

An enhanced effort counterfeit deterrent research and development program was established during fiscal 1980. New positions were created and position descriptions written to include areas where future program expertise will be required. While complete staffing of these positions has not been accomplished, the program has moved ahead in several areas. An evaluation was conducted on the use of a cellulosic substrate material as a carrier for authenticating information. Handsheets, of the current fiber finish, were made with several generic types of synthetic fibers incorporated into the sheet at various concentrations. This evaluation indicated that some synthetic fibers could be more easily incorporated into the sheet than others, and that there were limits on the concentrations. Contract research and development work on distinctive fibers continued with the U.S. Army Natick Laboratories to conduct a study on the feasibility of using photochromic materials as a security document authenticating feature. A contract was initiated with the Naval Research Laboratories to study the feasibility of using vacuum deposited materials as an authenticating and/or denominating feature on security documents.

During this period, a total of 25 cases were submitted for analysis by the U.S. Secret Service. There was only one occasion where expert testimony was actually required to support technical analyses performed.

#### Substrate research and development

Test printing of a plastic substrate was accomplished during fiscal 1980. As a result of Federal Reserve Board interest in the use of DuPont Tyvek as a currency substrate, extensive laboratory testing and practical press trials were conducted. When Tyvek was first tested 4 years ago, it was not possible to run it through the second intaglio printing. In the most recent press trial, however, both sides of the Tyvek were printed. While there are some inherent drawbacks associated with putting a plastic substrate through an intaglio press, the understanding of these problems will be of assistance in defining the properties that future plastic materials must have to be successful.

### Quality control

To correct a costly quality problem, i.e., bled trim currency notes (notes cut into the border requiring replacement), a new register control system was developed. During a practical trial of the system, the bled trim problem was reduced dramatically. Full implementation of the system in the currency program is expected to reduce costs by at least \$500,000 per year.

In concert with the development of the automatic currency inspection equipment, quality standards for currency have been developed. The objective of currency standards is to furnish guidelines which will provide the highest and most consistent quality level while preventing hypercritical examination, thereby reducing the costs of mutilating acceptable work. Training in the use of standards to existing manual examination has resulted in an increase in the yield of currency sheets by approximately 2 percent. Cost savings are estimated at \$500,000 per year.

Based on the results of various "at press inspections," a program has been developed to phase in quality control inspection at all major currency face presses. Early detection and resolution of quality problems is the objective of the plan. Earlier tests have shown positive effects on the yields of both currency sheets and notes.

### Internal audit program

The Audit Division conducts various types of financial, operational, managerial, and contractual reviews to assess the effectiveness and efficiency of performance, determine compliance with established laws, regulations, or management policies, and to evaluate the quality of various information systems and related internal controls. During fiscal 1980, 43 reports of audit were released containing recommendations for management action.

Substantial audit resources were provided to assist in defining requirements for a proposed financial management information system, evaluate proposed procedures and system changes, and follow up on the status of unresolved audit recommendations. The Division provided assistance on an Office of Management and Budget study of U.S. Government-owned gold at the Fort Knox depository. An auditor also served on the audit of the Exchange Stabilization Fund for the Secretary of the Treasury.

Audit results included the identification of potential monetary savings or cost avoidance of about \$132,000. In addition, numerous contributions to improving systems, procedures, internal controls, and debt collection were made. Many of these efforts resulted in substantially reducing opportunities for waste, fraud, or abuse.

The Internal Affairs Division was established in March 1980 to actively seek out areas of waste, fraud, abuse, and mismanagement, and to investigate allegations of illegal acts or employee misconduct. By September 30, two investigators had been hired to implement the program and two investigations of employee complaints initiated. The Division has participated in one investigation conducted by a representative of the Inspector General's Office. In addition, plans are being made to initiate surveys in fiscal 1981 to detect waste, fraud, abuse, and mismanagement and to recommend corrections or, where appropriate, to conduct investigations.

### Facility improvement

The air conditioning system in Photoengraving was completely modified to provide proper temperature, humidity, and dust control, thereby eliminating the cause for the loss of thousands of dollars work of defective plates each

month. Engineering specifications were prepared for the procurement and installation of new equipment for a complete power distribution network in the Annex Building. The new system will provide nearly twice the power presently available and eliminate the environmental hazard posed by the PCB contamination of the old transformers.

The Bureau's 5-year space plan is currently being implemented. A contract has been awarded to an architectural and engineering firm for the first phase of the plan; namely, the move of Research and Engineering to the Annex Building making space available for the installation of the new postage stamp coiling and examining equipment to be delivered in mid-1981. In addition, complete construction plans were prepared for the renovation of the auditorium to provide temporary office space.

Fabrication of the engineering prototype electronic currency inspection system was completed July 16, 1980, preliminary factory tests were successfully conducted during July and August 1980, and the system had been installed by yearend. This system will be used to evaluate electronic inspection technology to determine the most effective means of introducing this technology into the Bureau manufacturing operations, resulting in significant costs savings.

#### Security program

The security access control system has been updated with a compatible retrievable memory system which provides personnel audit trails throughout both buildings. Security and fire alarms, added to the system, will be annunciated in clear English text in both Lieutenants' offices as well as the emergency command center.

Design proposals have been prepared for badge-controlled turnstile entrances to five production areas. Once installation is completed, the requirement for a three-shift security officer will be eliminated, thereby effecting an expected savings of \$250,000.

The Bureau has tightened controls in respect to product accountability by establishing definitive, written procedures concerning the issue, receipt, transfer, and intra-intercomponent handling of security products before, during, and subsequent to their production. The accountability task force, appointed by the Director and consisting of both management analysts and industrial security specialists, has thus far published and integrated 13 chapters into the "Accountability Controls for Security Items" manual. The manual has been distributed to all operational components of the Bureau for their immediate use. Further task force accountability studies continue with a view towards the eventual automation of product accountability.

#### Data processing capability

The Bureau has embarked on the development of a sophisticated data processing capability with the intent of providing the latest state-of-the-art systems and concepts to support the accomplishment of the Bureau mission. Initial steps in this project have been the reorganization of the ADP Systems Division to provide a wider range of services to the various operating elements of the Bureau and the acquisition of data entry/terminal minicomputers which will effectively gather data at the source and provide for a distributed processing network.

Emphasis has been placed on upgrading the ADP personnel skills level so that innovative ADP systems may be evaluated and installed to support the Bureau.



### Occupational safety and health

A comprehensive occupational safety and health resource management program was developed and implemented in accordance with Federal statutory mandates and Treasury directives. During fiscal 1980, this program was highly successful and surpassed its original goal of reducing continuation of pay costs by 15 percent by achieving a cost reduction of more than 22 percent. Continuation of pay costs are funds paid to employees for up to 45 calendar days while they are recovering from traumatic injuries received on the job. While there were no significant reductions in the number of lost-time traumatic injuries from the previous fiscal year, the program was successful in significantly reducing the severity (number of days lost per injury) of the injuries. During fiscal 1980, the total number of days employees were paid continuation of pay was reduced by more than 60 percent from fiscal 1979. The successful implementation of the occupational safety and health resource management program resulted in demonstrable contributions to the efficiency and effectiveness of Bureau operations.

### Labor relations

The Bureau continues to foster constructive and harmonious relationships with its employees and the 17 bargaining units which represent them. In keeping with the spirit and intent of the Civil Service Reform Act of 1978 (CSRA), management deals with 16 AFL-CIO affiliate unions representing 25 distinct craft groups, a noncraft unit, and a guard unit. One independent union represents the General Schedule clerical/technical employees. Fifteen substantive negotiated labor-management agreements are presently in existence. Various provisions of these labor agreements are being revised as the Bureau strives to come into compliance with the CSRA.

The experiment in flexible and compressed work scheduling is continuing. Results thus far are extremely favorable. There has been a reduction in call-in occasions and the use of leave for doctor's appointments, etc. Feedback from participating employees is enthusiastic and encouraging.

### Training resource management system

A complete system was designed and implemented which identified training needs in concert with the performance evaluation process, determined how those needs would be met, allocated budgets for training and training-related travel to offices, and monitored expenditures. Subsequent modifications were made to improve the system, and all managers were briefed on the revised procedures.

### Interim performance appraisal system and merit pay

A performance appraisal system for merit pay employees was designed and piloted. Training sessions were held for all GS-13/15 managers, supervisors, and management officials, as well as for the executives who supervise them. After the system had been in effect for 6 months, a survey was distributed to both raters and ratees to get feedback on the implementation of the system for incorporation into the final merit pay appraisal system.

An interim managerial bonus plan was developed in conjunction with the interim performance appraisal system to reward managers for substantial accomplishments of their performance plans and resource plans.

### Executive development

The Bureau's Senior Executive Service candidate program was announced and two selections made. As core participants in Treasury's program, candidates have been scheduled to participate in many of the Department-sponsored programs. A new individual development plan process for all incumbent managers was developed and implemented on a 6-month pilot period following the training of all managers.

### Productivity improvement program

An organizational effectiveness/productivity improvement program plan was developed and approved by Bureau management. The plan addresses means to increase productivity and effectiveness through better utilization of the human resources of the Bureau. Organization development skills and methods are emphasized throughout the various components: Strategic planning, organizational assessment, action planning and problem solving, resolution of issues and cross-functional problems, implementation of action plans, and followup evaluation. In addition, quality circles, specific training activities, and other productivity improvement methods will be investigated for possible use in solving identified problems. The implementation of this total plan will begin in fiscal 1981.

### Incentive awards and suggestions

During fiscal 1980, suggestions approved for adoption included 6 with tangible first-year benefits of \$284,558, and 48 with intangible benefits. Awards for these suggestions were \$5,280 for the suggestions with tangible benefits, \$2,000 for the suggestions with intangible benefits, and three letters of commendation for awards with intangible benefits. One manager has been nominated to the Department for a Federal energy savings award for energy reduction by Bureau vehicles of nearly 37 percent.

There were 385 cash awards for sustained superior performance totaling \$67,467. Approximately 13 percent of the work force received an average award of approximately \$175. In addition, 29 employees, or approximately 1 percent of the work force, received quality salary increases.

### Employee counseling services program

Beginning in fiscal 1979, the Bureau initiated a comprehensive employee counseling services program, formalized in the spring of 1980, by approval of an agency regulation covering alcohol and drug abuse counseling and referral for diagnosis and treatment, with followup counseling and coordination with local rehabilitation agencies, and counseling for troubled employees in mental health, financial and family difficulties, and job-oriented interpersonal difficulty resolution. Within the present enrollment of 53 employees, nearly all levels of management and worker-level positions are included.

### Equal employment opportunity programs

In fiscal 1980, the Bureau implemented the new Federal guidelines for equal employment opportunity and affirmative action programs issued by the Equal Employment Opportunity Commission. Specific achievements were the internal recruitment of a seven-person plate printing apprenticeship class, which includes two women and three minorities, and the placement of a minority bookbinder. The apprenticeship will be expanded to two more crafts in fiscal 1981.

## OFFICE OF EQUAL OPPORTUNITY PROGRAM

The Office of Equal Opportunity Program assists the Assistant Secretary (Administration) in the formulation, execution, and coordination of the policies and programs related to providing equal employment opportunity for 125,000 Treasury employees nationwide. The Office guides and oversees the implementation of the Department's EEO program and affirmative action plans prepared by 11 component bureaus; provides for the implementation of the Federal Women's Program, the Hispanic Employment Program, the EEO program evaluation, and is responsible for the processing and adjudication of discrimination complaints from Treasury employees and applicants.

The following table provides a breakout of the Treasury work force by minority group status and grade groupings.

*Treasury employment by minority group status*

	1969	1973	1975	1978	1979	Comparison 1978-1979		Comparison 1969-1979	
						Number	Percent	Number	Percent
Total employees*	85,635	106,157	122,648	122,295	125,126	2,831	2.31	39,491	46.12
Black	12,251	16,170	19,533	19,882	21,989	2,107	10.60	9,738	79.49
Hispanic	1,116	2,788	3,912	4,670	5,236	566	12.12	4,120	369.18
Native American	85	146	192	186	200	14	7.53	115	135.29
Asian American	505	1,084	1,485	1,409	1,543	134	9.51	1,038	205.54
Other	71,678	85,969	97,526	96,148	96,158	10	.01	24,480	34.15
Total GS employees	79,858	99,839	111,205	112,007	114,925	2,918	2.61	35,067	43.91
Black	9,449	12,891	15,327	16,308	18,316	2,008	12.31	8,867	93.84
Hispanic	935	2,486	3,078	3,938	4,406	468	11.88	3,471	371.23
Native American	81	140	167	168	181	13	7.74	100	123.46
Asian American	475	981	1,287	1,272	1,390	118	9.28	915	192.63
Other	68,918	83,341	91,346	90,321	90,632	311	.34	21,714	31.51
Total GS 1-4	19,679	23,869	28,174	26,319	27,822	1,503	5.71	8,143	41.38
Black	4,948	5,932	6,664	6,452	7,606	1,154	17.89	2,658	53.72
Hispanic	300	922	1,168	1,424	1,628	204	14.33	1,328	442.67
Native American	26	45	57	42	49	7	16.67	23	88.46
Asian American	87	186	228	273	281	8	2.93	194	222.99
Other	14,318	16,784	20,057	18,128	18,258	130	.72	3,940	27.52
Total GS 5-8	21,603	30,793	33,064	34,178	35,359	1,181	3.46	13,756	63.68
Black	3,077	4,837	5,822	6,251	6,847	596	9.53	3,770	122.52
Hispanic	281	738	960	1,331	1,521	190	14.27	1,240	441.28
Native American	24	46	49	46	49	3	6.52	25	104.17
Asian American	139	394	437	439	514	75	17.08	375	269.78
Other	18,082	24,778	25,796	26,111	26,428	317	1.21	8,346	46.16
Total GS 9-12	28,737	32,615	36,639	37,250	36,934	-316	-.85	8,197	28.52
Black	1,257	1,769	2,406	3,046	3,252	206	6.76	1,995	158.71
Hispanic	316	709	820	1,021	1,078	57	5.58	762	241.14
Native American	27	40	47	65	69	4	6.15	42	155.56
Asian American	179	299	491	419	446	27	6.44	267	149.16
Other	26,958	29,798	37,875	32,699	32,089	-610	-1.87	5,131	19.03
Total GS 13-18	9,839	12,562	13,328	14,260	14,810	550	3.86	4,971	50.52
Black	167	353	435	559	611	52	9.30	444	265.87
Hispanic	38	117	130	162	179	17	10.49	141	371.05
Native American	4	9	14	15	14	-1	-6.66	10	250.00
Asian American	70	102	131	141	149	8	5.67	79	112.86
Other	9,560	11,981	12,618	13,383	13,857	474	3.54	4,297	44.95

\* Includes wage board personnel.

NOTE: Grade comparisons are for GS series only. Senior Executive Service totals (GS 16-18 prior to 1979) are included in 1979 GS 16-18 totals.

With the passage of the Civil Service Reform Act of 1978, and the receipt of new regulations from the Equal Employment Opportunity Commission and the Office of Personnel Management, the Department has made a number



of changes within its equal employment opportunity program to comply with new and changing requirements. Some of the most important changes follow.

In May 1980, Treasury's Department-wide affirmative action plan system was revised and reorganized into 127 plans which cover all of the Treasury facilities. The zero-base budgeting objectives EEO tracking system has been revised to provide management with a better analysis of the progress of affirmative action within the Department.

To strengthen the Hispanic Employment Program, a new directives manual chapter (TD 67-13.E, March 12, 1980) was issued outlining the policy and procedures for implementation of the program. Another directive (TD 67-13.F, May 1, 1980) was issued outlining procedures for implementing the Bilingual/Cultural Certification Program throughout the Department. This directive was intended to assist bureau headquarters and field offices in developing a program using bilingual and cultural certification as a tool for Hispanic recruitment and employment.

A new Federal Women's Program directive was issued (TD 67-13.D, October 19, 1979) which provides for the career development of women. A pilot training program was developed and implemented through the joint efforts of the Office of Personnel and the Office of the Equal Opportunity Program. It consisted of a series of 8 seminars—2 for 50 male managers, and 6 for 150 women employees in 3 grade groupings, GS 5-6, GS 7-12, and GS 13-15.

During the past year, the report of the Office of Personnel Management Task Force on Women in Law Enforcement was completed. This task force had among its members Treasury law enforcement women employees and Federal Women's Program managers from each Treasury bureau with law enforcement responsibilities. The dissemination of the report within the Department has resulted in increased emphasis on recruiting of women for the law enforcement field, the review and elimination of sex-stereotyped training films, and the utilization of women instructors in law enforcement training classes.

Because of the large number of discrimination complaints being filed at the bureau level, the departmental Complaints Processing Staff in conjunction with bureau staffs began field visits to those bureau facilities that have the highest incidence of EEO complaints.

## FEDERAL LAW ENFORCEMENT TRAINING CENTER

The Federal Law Enforcement Training Center was established as a bureau of the Department of the Treasury on May 2, 1970, and is under the supervision of the Assistant Secretary (Enforcement and Operations). Occupying 1,500 acres near the city of Brunswick, Ga., the Center serves as an interagency training facility for Federal law enforcement personnel.

The Department of the Treasury is the Center's parent agency, and as such exercises supervision over administrative and financial activities. Training policy, programs, and standards are established by an interagency Board of Directors, comprised of eight members representing the major agencies which have organizations participating in the Center. Five directors are voting members—one each from the Departments of Interior, Justice, and

Treasury; one from the General Services Administration; and one 2-year rotational seat (currently the Department of Housing and Urban Development) representing the several other participating organizations with less than 500 law enforcement officers. Three directors are nonvoting members—one each from the Office of Management and Budget, the Office of Personnel Management, and the U.S. Capitol Police Board.

During fiscal 1980, the Center's Board of Directors approved an exception to its established policy of providing training for only enforcement personnel with arrest and weapon-carrying authority. The Board approved experimental programs to train regulatory enforcement personnel of the Bureau of Alcohol, Tobacco and Firearms and the U.S. Customs Service. This departure from normal participation eligibility criteria was permitted in order to allow optimum use of resources, eliminate costly duplication of similar functions, and enhance the effectiveness of training for these personnel. This training was conducted on a space-available, reimbursable basis, and no significant operational problems were encountered during the experimental period. The Center is conducting an analysis of this experiment and will submit its findings to the Board. Early results of the analysis indicate that a recommendation will be made to continue the expansion of law-enforcement-related training activities, subject to restraints which insure that priority is given to programs for personnel directly engaged in criminal investigation and police operations.

During fiscal 1980, the question of where to conduct training for personnel of the Drug Enforcement Administration (DEA), a matter which has been examined several times in recent years, was addressed by DEA and the Center. A study team comprised of DEA and Department of Justice representatives issued a report which served as the foundation for their recommendation to relocate DEA's basic criminal investigator training to the Center beginning in fiscal 1982. This proposal will be submitted to the Center's Board of Directors for its consideration during early fiscal 1981. The Center anticipates that approximately 100 DEA special agent recruits would participate in the Center's basic criminal investigator program on an annual basis. Further discussions and negotiations between the Center and DEA will serve as the basis for future decisions regarding the feasibility of relocating additional DEA training activities such as specialized basic and inservice programs.

At the end of fiscal 1980, personnel of 36 law enforcement organizations, representing all branches of the Federal Government, were participating in the Center's programs. During the year, 9,000 students graduated from the Center, representing a 10-percent increase over fiscal 1979. Student-weeks of training increased by 10 percent.

#### Training programs

*Basic training.*—The basic training programs for recruit investigators and officers are conducted by the Center staff and range in length from 5 to 16 weeks. During fiscal 1980, 18 basic 7-week criminal investigator classes were conducted, graduating 650 students. This represents an increase of 6 percent, or 40 students, over the previous fiscal year. The basic programs for police officers graduated 1,900 students, resulting in an increase of 10 percent over the previous year. A total of 2,550 students graduated from all basic programs—an increase of 9 percent over fiscal 1979. The student-weeks of training presented in the basic programs experienced an increase of 8 percent.

The Center's training staff and faculty continued to improve the existing programs and began the development of several new programs during the

year in order to meet changing training requirements. These included the development of new procedures to ensure examination integrity, development of a computer fraud instructional unit, and experimentation with a new system of assigning instructors as class coordinators/faculty advisers. A curriculum review conference was held in April 1980 with organizations which participate in the recreation-land management program. This conference resulted in significant curriculum modifications and improvements to this 9-week program. In addition, modifications were made to the basic program for U.S. Customs Inspectors, integrating instruction in their specific responsibilities with the instruction in general law enforcement subjects taught by Center faculty.

Work continued on a comprehensive job and task analysis that will identify the basic tasks, conditions, and standards applicable to all law enforcement officer positions in all participating organizations. The results of this analysis will be used to further validate the current programs and initiate any needed changes. This analysis corresponds to the continuing study to develop job-oriented and validated physical efficiency tests for law enforcement personnel. In addition, a study was initiated to validate critical tasks for driving skills as they relate to law enforcement operations. Extensive studies and experiments resulted in significant changes to the methods and procedures used in firearms training. The new methods include increased use of the "transitional target," recently developed by the firearms faculty, and procedures were designed to place greater emphasis on the student's performance in practically oriented exercises and tests.

The Center maintained close liaison with the Inspectors General (IG) of the various departments and agencies to help them identify training requirements and appropriate training programs. Center officials participated in a task force committee established by the IG Council to determine various options available for training both investigators and auditors. The Center anticipates that during fiscal 1981, greater progress will be made toward implementation of training courses to accommodate the developing needs of the IG community. During fiscal 1980, IG employees continued to participate in the white collar crime seminars and the criminal investigator basic training program.

*Common advanced, inservice, refresher, and specialized training (CAIRS).*—In addition to basic training, the Center conducts advanced and specialized training for veteran investigators and officers in subjects common to two or more organizations. During fiscal 1980, these CAIRS programs accounted for 1,300 graduates and 2,000 student-weeks of training.

This represents a 125-percent increase in graduates which resulted primarily from the 100-percent increase in students who participated in the 2-week white collar crime seminar. This program was developed and first conducted in fiscal 1979 in response to the expressed needs of the participating organizations. The additional emphasis now being placed on the investigation and prosecution of fraud and other financial crimes highlights the need for training in this area. Slight increases in graduates were also achieved in other CAIRS programs, which included advanced law enforcement photography and various instructor training courses.

A new CAIRS program in wildland fire investigation was close to completion at the end of fiscal 1980. This program is being developed at the request of several organizations engaged in the investigation of suspected arson activities in the Nation's forests and wildlands. It is expected that the development of the program will be completed and available for consideration by the organizations and the Board of Directors in early fiscal 1981.



*Agency advanced, inservice, refresher, and specialized training (AAIRS).*—The Center offers each participating organization the opportunity to develop and conduct advanced or specialized training to meet the specific needs of its personnel. This training is conducted by personnel of the organization, with assistance provided by Center faculty when available. However, all administrative and logistical support for the training is provided by the Center. This unique arrangement allows participating organizations to meet their individual training requirements and, at the same time, benefit from improved facilities and the cost savings available through consolidation. A total of 6,200 students graduated from AAIRS programs in fiscal 1980, for a slight increase over the previous year. The majority of the programs were conducted by organizations of the Departments of Interior, Justice, and Treasury.

At the close of the fiscal year, members of the Center's staff and representatives of participating organizations were jointly developing plans to modify facilities at the outdoor firing ranges to accommodate more realistic handgun and shotgun training as part of several AAIRS programs. This activity is in direct response to requests by several of the organizations.

#### Training support

The addition of new programs and the modification of existing programs during fiscal 1980 required the training support activities of the Center to adapt to changing requirements. This was accomplished with increased productivity resulting in several areas. The reorganization of the Center's staff, which occurred during the year and is described in the "Management improvement" section of this report, consolidated several support activities into one division.

The addition of computerized typesetting equipment resulted in a productivity increase of 40 percent in preparation of artwork for printed materials. An increased workload and productivity improvements made possible a production level for all graphic arts activity of 140.6 percent above accepted standards. Quality control measures were added to the photographic processing activity, and resulted in improved and consistently high quality products. In addition, the increased demand for photographic service required that a substantial portion be contracted to private firms.

The television production staff continued to assist instructors and administrators in the development and refinement of television as a valuable teaching tool. This included providing training to 28 instructors in the use of video-tape equipment for practical training exercises. The Center has expanded the use of video-tape equipment in several programs, which has resulted in improving the evaluations and critiques of student performance. Assistance was also provided to participating organizations in the production of a number of video tapes for use in their training. The study to compare the cost-effectiveness of in-house television production with reliance on private contractors for the service was continuing as the fiscal year ended.

The completion of new facilities during the year required their incorporation into the scheduling system. This occurred with a minimum of disruption to normal training activities and has resulted in more efficient use of space and facilities. The new classroom building was equipped with modern audiovisual systems, and staff members were trained in their use and maintenance. The Center's Learning Resources Center was transferred to this same building and is conveniently available to staff and students for reference and research activities. Use of the Center's word processing unit received strong management support during the year, increasing its output by 100

percent and resulting in a substantial savings of administrative and clerical workload.

The student recreation program continued to expand and diversify, with twice the number of students participating during fiscal 1980 as in the previous year. Many of these recreation activities were funded through nonappropriated funds generated by the Center's Employee Recreation Association. They included team and individual competitions and tournaments in a variety of athletic activities, indoor games such as backgammon and bridge, weekend trips to nearby points of interest such as Walt Disney World, and live entertainment in the Student Center.

#### Administration

Several of the Center's administrative activities were streamlined during fiscal 1980. These included conversion of property management records from a manual keypunch to a computerized system, which provides more efficient processing and retrieval of information. In addition, employee time and attendance submissions were converted from a manual system, transmitted via mail, to the Treasury payroll/personnel information system terminal, which utilizes a direct ADP input system. This conversion results in faster processing of leave and premium pay data. Installation of Southern Bell's Dimension 2000 telephone system throughout the Center was completed during fiscal 1980, which resulted in reduced monthly costs for telephone service and simultaneously improved telephone capabilities and features. The demand for printing and reproduction services increased by 37 percent over fiscal 1979. This was due to expanding training activities, with the majority of the increase related to support of the white collar crime seminar.

The workload required to maintain the Center's facilities experienced a large increase during fiscal 1980, as construction of new buildings was completed and they were occupied. This increased workload was accommodated through a staff reorganization of the Facility Engineering and Maintenance Division. Personnel were assigned to specific work areas and/or teams to decrease manpower and transportation requirements. Personnel are also being cross-trained in a variety of traditional crafts to further increase flexibility and productivity.

Personnel management was a very active area for the Center during fiscal 1980. A performance appraisal system was designed to meet the criteria of the Civil Service Reform Act of 1978, with numerous training sessions conducted for supervisors and managers regarding the development of job elements and performance standards. The Center's equal employment opportunity recruitment program was revised in accordance with guidelines established by the Equal Employment Opportunity Commission, and procedures were developed to determine areas of underrepresentation of minorities and allow redirection of recruiting activities. During the year, 22 students participated in the Center's undergraduate intern program and 1 student completed the requirements for an advanced degree under the graduate intern program. In June 1980, the Center held its first annual awards ceremony to recognize individuals and organizational units that performed major roles in the successful completion of the construction, reorganization, and relocation activities. The faculty enrichment program was continued and expanded during the year to invite national and international leaders in law enforcement and related fields to visit the Center to lecture and lead informal discussions among faculty members.

### Management improvement

A reorganization of the Center staff was accomplished during fiscal 1980. The major features of the reorganization were the consolidation of criminal investigator and police faculties and the creation of separate offices for Program and Faculty Management. This provides increased flexibility in instructor assignments, allows exposure of instructors with outstanding credentials and expertise to all basic students, and establishes one office to serve as the Center's liaison with participating organizations regarding training programs.

A study was underway at the close of fiscal 1980 regarding instructor self-evaluation and improvement. The results of the study are expected to yield procedures and criteria to guide instructors in increasing their productivity, already at a commendable level. In addition, development was proceeding on a new Duty Officer concept which, when implemented, will result in improved informal communication and exchange between instructors and students and enhance the learning environment for students.

An experimental program in alternative work schedules for staff members was initiated during the year. The program is designed to allow supervisors and employees to schedule work hours to coincide with fluctuations in work requirements, and is expected to result in increased productivity. The success of the program will be evaluated after 1 year in order to determine whether it should continue.

There were significant changes in management positions during the year, with the selection of personnel to fill the Deputy Director and three new Assistant Director positions created by the reorganization. These major changes in the organization and key personnel have improved the Center's ability to meet the changing training needs, increase productivity, and improve the cost-effectiveness of training.

### Training and support facilities

During fiscal 1980, the Center accepted operational control over most of the major projects in the master plan construction program. These included a new classroom building to house activities for basic training programs; expansion of existing facilities and new construction in the Physical Specialties Complex to provide indoor training stations, classrooms, and equipment issue area, additional driver specialties facilities such as a control tower, highway response course, and defensive driving course; and renovation of the existing classroom building to provide behavioral science laboratories, driver specialties classrooms and offices, and a more energy-efficient heating and cooling system. Work was also completed on new paving, a new energy distribution system, an improved water/sewer system, a central fire alarm system, and a portion of the outdoor lighting system. Another project undertaken and completed during the year was increasing the security of the weapons storage areas at the outdoor firing ranges.

It is expected that the few remaining projects in the master plan construction program will be completed in early fiscal 1981. When completed, the adaptation of the former Glynco Naval Air Station for use by the Center will result in not only significant savings in construction expenditures, but also creation of excellent facilities in which to train the Nation's law enforcement personnel.

A comprehensive energy conservation program was initiated during fiscal 1980, and received strong management endorsement and support. All training programs were reviewed to eliminate any unnecessary use of vehicles. This was accomplished by using alternate means of transportation and realigning



sequence of courses, and did not affect the quality of the programs. A driver energy conservation awareness training program was begun for all staff members, and instruction in energy conservation techniques was incorporated into driver specialties training. Bicycles were purchased and used by staff members, rather than automobiles, for transportation between locations on the Center. The completion of the construction program eliminated the requirement to provide transportation for students between various locations on the Center, and a "walking campus" concept was implemented. In addition, natural gas is now being used in heating plants to the maximum extent possible to reduce electric power requirements. The Center began participating in energy conservation programs sponsored by the Department of Energy (DOE) in fiscal 1980, including the purchase of six electric vehicles. Delivery of the vehicles is expected in early fiscal 1981 and they will be used for transportation between locations on the Center in lieu of automobiles. Also, a DOE grant was obtained during the year to provide solar heating for the new aquatic training facility.

## FISCAL SERVICE

### Bureau of Government Financial Operations

The functions of the Bureau are Government-wide in scope. The Bureau disburses by check, electronic funds transfer, or other means of payment for most Government agencies; settles claims involving loss or forgery of Treasury checks; manages the Government's central accounting and financial reporting system by drawing appropriation warrants, by maintaining a system of accounts integrating Treasury cash and funding operations of disbursing and collecting officers and of Government program agencies including subsystems for the reconciliation of check and deposit transactions, and by compiling and publishing reports of budget results and other Government financial operations. The Bureau also provides banking and related services involved in the management of the Government's cash resources; under specified provisions of law is responsible for investing various Government trust funds; oversees the destruction of currency unfit for circulation; provides central direction for various financial programs and practices of Government agencies; and directs a variety of other fiscal activities.

#### Disbursements and check claims

During fiscal 1980, the Division of Disbursement operated 11 disbursing centers servicing over 1,600 Federal administrative offices throughout the United States and in the Philippines. The Division also rendered disbursing services for embassies located in Central America, South America, and the Far East. In addition to its disbursement activities, the Division prepared and distributed Federal tax deposit forms for the Internal Revenue Service.

*Management improvements and significant achievements.*—Increased savings continue to be realized from the presorting program which started in 1976. To obtain a 2-cents-per-item postage discount for those items that qualify, checks are sorted into ZIP code sequence, placed in trays labeled to the 5-digit or 3-digit postal destinations, and released to the Postal Service thus

permitting direct shipment to the delivery points. In addition to the major classes of payment already being presorted, civil service annuity checks and series H savings bond interest checks were added to the program in fiscal 1980. The Division is presorting each month an average of 32 million social security, supplemental security income, veterans compensation and pension, veterans education, Railroad Retirement and Veterans employee salary checks, as well as approximately 61 million tax refund checks during the peak period of February through June. The net savings realized from presorting in fiscal 1980 was \$7,784,650.

The Division of Disbursement converted processing of Railroad Retirement Board nonreceipt claims from the manual operation to a magnetic tape system in fiscal 1980. Stop payment and photocopy requests for social security, supplemental security income, veterans, railroad retirement, and income tax refund programs processed under the tape claims system totaled 759,818, or approximately 57 percent of the total stop payments during the year. The Division also completed programming and testing for inclusion of claims against Office of Personnel Management payments to the tape claims system in fiscal 1981.

Extension of the electronic funds transfer system (EFT) to Federal salary payments was begun in September 1978, and by the end of fiscal 1980, eight Federal salary payroll conversions had taken place. Forty-one more agencies are expected to convert prior to January 1982. The EFT salary program is replacing the composite check program.

An automated claims/after payment action system is currently under development for implementation on the new computer equipment to be installed at disbursing centers beginning in fiscal 1981. This standard system is expected to facilitate the responsiveness of the Treasury to claims of payment nonreceipt, and to expedite the reclamation process for both check and EFT payments. These objectives will be accomplished through the capability to process more claims through the automated system, to automatically research and verify claims for an increased number of payments, and to computer generate and control EFT reclamation and trace actions processed at the disbursing centers. Interim enhancements to the claims system in fiscal 1980 are the computer generation of EFT reclamation claims on pinfeed forms in five disbursing centers, resulting in savings of many man-hours needed for claims processing. Also, following a 4-month test, automatic followup on EFT claims was discontinued.

The Division of Disbursement completed a feasibility study involving the acquisition of new computer output microfilm (COM) equipment to replace older equipment acquired in the early 1960's. An award was made for two COM recorder systems and two new microfilm duplicators to be installed in early fiscal 1981. Microfilm provides a permanent record of check issues and is used for processing check claims and inquiries received from claimants in other Government agencies. Disbursing centers submit the magnetic tapes containing issue record information to the Chicago Disbursing Center for centralized microfilming. The purchase cost of the new COM and duplicator equipment is less than \$300,000. Eight-year system's life cost savings by upgrading the current microfilm equipment and operating procedures is approximately \$1 million.

A Paper Check Task Force has been formed to resolve all major issues involved with converting the Treasury card check system to a paper check system. The task force is developing comprehensive plans involved with the study including milestones, major activities and problems to be addressed, training, etc. A tentative target date of August 15, 1981, has been established

to complete the feasibility and cost analysis and to describe in detail how the system would function.

*Disbursing operations.*—During fiscal 1980, a total of 711,238,309 checks, savings bonds, adjustments and transfers, and EFT payments were issued under Treasury's centralized disbursing system at an average cost of \$0.0483. In addition, 126,282,503 Federal tax deposit forms were prepared and mailed.

The following table is a comparison of the workload for the fiscal years 1979 and 1980:

Classification	Volume	
	1979	1980
Operations financed by appropriated funds:		
Checks and electronic funds transfers:		
Social security benefits .....	397,000,003	406,173,824
Supplemental security income payments .....	51,803,361	51,240,543
Veterans benefits .....	73,423,603	72,015,398
Income tax refunds .....	69,616,637	74,851,275
Veterans national service life insurance dividends .....	2,820,338	2,762,615
Other .....	72,783,088	82,900,437
Savings bonds .....	7,534,414	5,081,162
Adjustments and transfers .....	228,225	156,045
	<u>675,209,669</u>	<u>695,181,299</u>
Operations financed by reimbursements:		
Railroad Retirement Board .....	13,591,797	13,819,028
Bureau of the Public Debt (General Electric Co. bond program) .....	1,920,331	2,237,982
Total workload—reimbursable items .....	<u>15,512,128</u>	<u>16,057,010</u>
Total workload .....	<u>690,721,797</u>	<u>711,238,309</u>

*Check claims operations.*—The Division of Check Claims adjudicates and settles claims against the U.S. Government for the proceeds of Treasury checks that are not received, lost after receipt, or which bear forged endorsements.

Substitute checks are issued when the check in question is determined to be outstanding at the time the claim is received.

Settlement checks are issued to payee/claimants when the original checks are found to be paid over forged endorsements, and to financial institutions or second endorsers when Treasury recovers the amounts of questioned checks through the bank reclamation system and later recovers the amounts from the forgers or when a U.S. Secret Service investigation determines that the payee/claimants actually cashed the questioned checks.

Settlements with agencies are made through voucher transactions with transfer of funds from one appropriation to another. Settlement credits to agencies are used when the agency notifies Treasury that the payee was deceased prior to the check date and the estate is not entitled to the proceeds of the check. Upon successful reclamation from the presenting or cashing bank the proceeds are credited to the agency's appropriation. Settlement debits to agencies' appropriations are the result of substitute checks being issued, on claims of nonreceipt, when the original checks are determined to be outstanding, and later, both checks are paid, thereby creating "double payment" cases. When Treasury and the agency have a formal chargeback agreement, the amount of one of the checks is debited against the agency's appropriation. When there is no chargeback agreement, Treasury must pursue collection from the individual or request the agency to collect the amount for Treasury. The double payment items are currently handled under



a manual system. An automated system that will facilitate cash flow to the Treasury is being designed.

*Reclamation activities.*—The purification of the preautomation bank reclamation files is continuing and in July resulted in the collection of \$338,130 from the Bank of America. The amount covered 1,200 out of 1,800 reclamations outstanding prior to August 1978, when the reclamation system was automated. Special emphasis is now being placed on collection of these items by furnishing the banks with computer listings of the outstanding reclamations. In early fiscal 1981 the larger banks will be notified that litigation will be pursued on checks that they cashed upon forged or unauthorized endorsements, if not refunded, based on preliminary findings by Treasury and the Department of Justice. These outstanding items will be placed under an automated control system as the purification of the file progresses.

*Financial accounting and reporting.*—Phase I of the financial accounting and reporting system was implemented to provide fiscal and operational control over the double payment accounts receivable, accounting documents, and transactions, and to provide management information, i.e., aging of receivables. All other manually maintained accounts in the Division will be absorbed as other phases of the system are implemented.

*Paperwork simplification.*—Paperwork simplification was a fiscal 1980 internal effort to expedite the manual claims-processing system by eliminating unnecessary paper handling and improving the workflow. The analysis of 3 manual systems has resulted in 74 recommendations for improvements, which are now in various stages of implementation. The remaining manual systems are in various stages of analysis and should be completed by mid-fiscal 1981.

*Forms of endorsement on Treasury checks.*—In fiscal 1979 proposed regulations concerning forms of endorsement on Treasury checks were published in the Federal Register for public comment. On January 4, 1980, a final rule on forms of endorsement was published and 31 CFR 240 was revised to reflect the acceptable endorsements. Treasury is now in the process of revising the wording on the reverse of U.S. Treasury checks to call public attention to the regulation change.

The following table shows the Division of Check Claims workload for fiscal 1980.

Classification	1980 volume
Nontape stop payment requests .....	256,334
Division of Check Claims substitute checks authorized (paper stops).....	105,791
Payee/endorser settlements authorized.....	37,637
Agency settlement credits authorized.....	30,610
Other settlements authorized.....	30,523
Reclamation requests to banks.....	106,783
Reclamation recoveries .....	92,189
Investigative referrals to Secret Service .....	60,434
Double payment intercepts.....	104,999
Double payment chargebacks to agencies .....	55,048
Cases closed.....	164,996
Agency paid-check photocopy requests .....	114,527

#### Government-wide accounting

*Government accounting systems.*—The Treasury financial communications system (TFCS) has been in operation since September 1976, and during fiscal

1980 processed \$70 billion in deposit transactions and \$56 billion in payment transactions. Utilizing a computer link to the Federal Reserve Bank of New York, TFCS provides access to the Federal Reserve Communications System and its associated financial data. TFCS automates the generation of nonrecurring payments and the receipt of Government deposits, and provides a comprehensive accounting and audit control mechanism for streamlining financial recordkeeping and reporting. As of September 1980, three Federal Reserve banks had implemented the letter of credit-TFCS system. In conjunction with the LOC-TFCS, an agency/TFCS terminal interface called LMRAS (letter of credit message retrieval and authorization subsystem) was implemented in April 1980. One major feature of LMRAS is that it allows an agency to perform the preaudit of letter of credit transactions in a reliable and timely manner.

On September 4, 1980, Treasury redeemed in full the outstanding gold certificates, series of 1934, which were issued only to Federal Reserve banks. Simultaneously, an equal amount of nondefinitive (book entry) gold certificates were issued to the Board of Governors of the Federal Reserve System. This changeover not only consolidated Treasury's gold liabilities into a single account but also extended the trend toward replacing definitive debt instruments with book entries. However, in recognition that destruction, or storage in a Treasury vault, of gold certificates, series of 1934, would not permit ready access by historical researchers, numismatists, and the general public, special custodial arrangements were made with Federal Reserve banks to allow display of the certificates in their numismatic museums. Thus, these certificates are now being held by the Federal Reserve Banks of Atlanta, Cleveland, Kansas City, Minneapolis, New York, Philadelphia, and Richmond and by the Smithsonian Institution in Washington, D.C.

In compliance with Public Law 95-630, American Arts Gold Medallion Act, a memorandum of understanding setting forth the procedures for accomplishing sales of gold medallions to the general public was approved by the Fiscal Assistant Secretary on June 9, 1980. These sales, which are being administered by the Bureau of the Mint, commenced on July 15, 1980.

*Assets and liabilities in the account of the U.S. Treasury.*—Table 53 in the Statistical Appendix shows the balances at the close of fiscal years 1979 and 1980 of those assets and liabilities comprising the account of the U.S. Treasury. The assets and liabilities in this account include the cash accounts reported as the "operating balance" in the Daily Treasury Statement. Other assets included in the account of the U.S. Treasury are gold bullion, coin, coinage metal, paper currency, deposits in Federal Reserve banks, and deposits in commercial banks designated as Government depositories.

Treasury's gold balance was \$11,227.7 million at the beginning of the fiscal year and \$11,168.4 million at yearend.

Stocks of coinage metal stood at \$295.5 million at the beginning of fiscal 1980 and \$325.4 million at yearend. Such stocks included silver, copper, nickel, zinc, and alloys of these metals which are not yet in the form of finished coins.

The number of depositories of each type and their balances on September 30, 1980, are shown in the following table:

Depositories	September 30, 1980	
	Number of accounts <sup>1</sup>	Balance
Federal Reserve banks and branches .....	37	<sup>2</sup> \$5,452,985,674
Other depositories reporting directly to the Treasury:		
Special demand accounts .....	87	29,576,262
Other:		
Domestic .....	10	3,057,539
Foreign <sup>3</sup> .....	33	2,435,427
Depositories reporting through Federal Reserve banks:		
General .....	1,113	51,209,534
Special (Treasury tax and loan accounts) .....	14,117	16,887,823,406
<b>Total .....</b>	<b>15,397</b>	<b>22,427,087,842</b>

<sup>1</sup>Includes only depositories having balances with the U.S. Treasury. Excludes those designated to furnish official checking account facilities or other services to Government officers but not authorized to maintain accounts with the Treasury. Banks designated as general depositories are frequently also special depositories, hence the total number of accounts exceeds the number of banks involved.

<sup>2</sup>Includes checks for \$1,351,109,392 in process of collection.

<sup>3</sup>Primarily branches of U.S. banks and of the American Express International Banking Corp.

Government officers deposit moneys which they have collected to the credit of the U.S. Treasury at Federal Reserve banks or at designated Government depositories, domestic or foreign. Certain taxes are also deposited directly by the employers or manufacturers who withhold or pay them. All payments are withdrawn from the U.S. Treasury account.

Cash deposits and withdrawals affecting the Treasury's operating balance are summarized in the following table for fiscal 1979 and 1980.

*Deposits, withdrawals, and balances in the U.S. Treasury account*  
[In millions of dollars]

	Fiscal 1979	Fiscal 1980
Operating balance at beginning of period .....	22,444	24,176
Cash deposits:		
Gross tax collections (selected) .....	465,722	523,687
Public debt receipts .....	492,757	589,228
Other .....	70,925	79,712
Total cash deposits .....	1,029,404	1,192,627
Cash withdrawals:		
Public debt redemptions .....	478,417	545,517
Letter of credit transactions:		
Medicare .....	27,611	33,278
HEW grants .....	30,920	36,707
Unemployment insurance .....	8,579	14,213
Other .....	482,145	566,098
Total cash withdrawals .....	1,027,672	1,195,813
Operating balance at close of period .....	24,176	20,990

*Investments.*—The Secretary of the Treasury, under specific provisions of law, is responsible for investing various Government trust funds. The Department also furnishes investment services for other funds of Government agencies. At the end of fiscal 1980, Government trust funds and accounts held public debt securities (including special securities issued for purchase by major trust funds as authorized by law), Government agency securities, and securities of privately owned Government-sponsored enterprises. See the



Statistical Appendix for tables showing the investment holdings by Government agencies and accounts.

*Issuing and redeeming paper currency.*—The Treasury is required by law (31 U.S.C. 404) to issue U.S. notes in amounts equal to those redeemed. In order to comply with this requirement in the most economical manner, U.S. notes are issued only in the \$100 denomination. U.S. notes represent only a very small percentage of the paper currency in circulation.

Federal Reserve notes constitute over 99 percent of the total amount of currency. The Bureau of Engraving and Printing prints and holds these notes in a reserve vault until needed by the Federal Reserve banks. The Bureau of Government Financial Operations accounts for Federal Reserve notes from the time they are delivered to the reserve vault by the Bureau of Engraving and Printing until redeemed and destroyed.

A comparison of the amounts of paper currency of all classes, issued, redeemed, and outstanding during fiscal years 1979 and 1980 follows:

[In thousands]

	Fiscal 1979		Fiscal 1980	
	Pieces	Amount	Pieces	Amount
Outstanding beginning of period .....	9,042,425	\$110,192,519	9,712,331	\$123,058,945
Issued during period .....	3,670,387	32,141,803	3,784,312	36,146,614
Redemptions during period .....	3,000,481	19,275,377	3,172,310	21,320,247
Outstanding end of period .....	9,712,331	123,058,945	10,324,323	137,885,312

Details of the issues and redemptions for fiscal 1980 and of the amounts outstanding at the end of the year are given by class of currency and by denomination in a table in the Statistical Appendix. Other tables in that volume give further information on the stock and circulation of currency and coin in the United States.

*Data processing.*—During fiscal 1980, 680.1 million checks were paid and reconciled by the electronic check payment and reconciliation system. These include all checks issued worldwide by civilian and military disbursing offices. A major computer system upgrade was accomplished with the last quarter installation of an IBM 4341 electronic digital computer which replaced two second-generation and two early third-generation computer systems. The check payment and reconciliation system was totally converted from second- to third-generation equipment, i.e., IBM 7074 to IBM 4341.

Continued improvements were made to the automation of the central accounting and public monies systems by completing the implementation of all remaining systems on state-of-the-art ADP equipment. The public monies system, which processes FRB transcripts, has been completely converted from second- to third-generation equipment and is now fully operational on the IBM 4341. The central accounting system, which consolidates and summarizes all of the cash transactions of the Federal Government, has all report cycles operational on the IBM 4341, with the last of the transaction-processing cycles scheduled for implementation commencing with fiscal 1981 data.

The intercept master file was reformatted based upon requirements created by a reorganization within the Division of Check Claims. Extensive efforts were made to identify and define requirements and priorities for claims processing.

#### Banking and cash management

*Foreign currency management.*—Important strides were realized by broadening of activities to include involvement, at the earliest stage possible, in

the cash management impact of funding procedures contained in international contracts. The general guidelines for this new effort were published on June 4, 1980, I TFRM 6-8065, "Restrictions on Financial Transactions with Foreign Countries and International Organizations." The long-range goal of these efforts will be to delay the outflow of funds from the Treasury. In fiscal 1980, the Foreign Currency Staff assisted various U.S. Government agencies in implementing these guidelines.

The staff also implemented new cost-effective worldwide banking arrangements for meeting U.S. Government needs. As a result of the use of competitive bidding procedures, important improvements in the acquisition and investment of foreign currencies were realized.

*Treasury tax and loan investment program.*—During fiscal 1980, the Treasury received interest revenues under the investment program totaling \$882.5 million. Fees paid to depositaries during the period for processing Federal tax deposits totaled \$27.4 million. To ensure the continued smooth operation of the program, procedural reviews were conducted for the fiscal operations supporting the program at the Boston, Philadelphia, Atlanta, Kansas City, Dallas, and San Francisco Federal Reserve Banks.

A two-phase study was completed on the adequacy of the 50-cents-per-item fee paid depositaries for processing FTD's. Phase one consisted of a review of processing procedures for FTD's at depositaries to develop an efficient standard processing model. In phase two, the Bureau commissioned, under competitive bid, the certified public accounting firm of Arthur Young and Co. to complete an independent determination to cost the model established under phase one.

*Cash management policy.*—I TFRM 6-8000, which prescribes cash management procedures to be observed by all Government entities whose financial transactions affect the cash account of the Treasury, was revised on June 4, 1980, to further refine and improve Federal cash management practices. Major revisions provide for payment due dates for amounts owed the Government of less than 30 days, current percentage rates for late charges on overdue payments (to be periodically disseminated through TFRM bulletins), criteria for authorized scheduled payments of delinquent accounts, payment terms included in contracts and procurement arrangements, criteria in determining cost-effective cash discounts, and new requirements on financial transactions with foreign countries and international organizations.

The report summarizing the findings and recommendations of the President's Reorganization Project on Strengthening Federal Cash Management was finalized in June 1980. The project, conducted throughout fiscal years 1978 and 1979, looked to Treasury's Fiscal Service for support in its efforts to improve agency cash management practices; it also provided a receptive arena to Treasury's cash management regulations.

*Paying grants through letters of credit.*—At the close of fiscal 1980, 90 Government agency accounting stations were financing with letters to credit under the Federal Reserve bank system. During the period the Bureau processed 158,564 withdrawal transactions aggregating \$85.5 billion, compared with 146,788 transactions totaling \$77 billion in fiscal 1979.

On September 30, 1980, 87 Government agency accounting stations were financing with letters of credit under the Treasury regional disbursing office system. During the year, Treasury regional disbursing centers issued 103,432 checks totaling \$26.6 billion, in response to grantee requests, compared with 85,522 checks totaling \$20.8 billion in fiscal 1979. These figures include 706 payments made under the LOC/TFCS totaling \$1.1 billion made under two of the above agency accounting stations.

*Destroying unfit currency.*—Forty-eight REI/CVCS currency processors have been installed and approved by Treasury for use at Federal Reserve banks to authenticate, account for, and destroy unfit Federal Reserve notes. As a result of an improved counterfeit detector developed by TEKNEKRON, all previously installed REI machines will be retrofitted with the new detectors commencing in early fiscal 1981. REI is the sole supplier of high-speed currency-processing equipment. Other prototype transport systems showed promise, but were not pursued for various technical or contractual reasons. Plans for the development and implementation of second-generation equipment are currently being discussed.

*Processing mutilated currency claims.*—During fiscal 1980, more than 47,200 mutilated currency claims were received and over \$10 million was paid out in settlement of claims. At the end of the year, about 200 cases remained unprocessed. The average case backlog during the year has been reduced from 7 to 5 months. Most of the backlogged cases are classified as "difficult" because of the degree to which the currency has been burned or mutilated, and the considerable amount of time required to process them.

*Accelerating receipt availability.*—During fiscal 1980, the Banking Staff, by emphasizing the use of wire transfers over TFCS and the establishment of competitive depository arrangements, accelerated the availability of the Government's collections resulting in imputed interest savings of \$150.3 million. The staff also assisted the Bureau of Alcohol, Tobacco and Firearms in developing proposals requiring payers of alcohol and tobacco excise taxes of \$5 million or more per year to use the TFCS. This action will accelerate the availability of approximately \$7 billion annually by a minimum of 3 days.

*Depositories and financial agents of the Government.*—Pursuant to Public Law 95-147, October 28, 1977, title 31, part 202 of the Code of Federal Regulations was rewritten to broaden the classes of financial institutions that may be designated as "depositories and financial agents of the Government." This designation, which heretofore applied only to banks insured by the Federal Deposit Insurance Corporation, will now include federally insured savings and loan associations and credit unions, and savings banks, savings and loans, building and loans, homestead associations (including cooperative banks), and credit unions insured by a State or agency thereof.

The law makes it possible for these institutions to maintain official accounts of Government officers who are authorized, for specific purposes, to have funds outside of the Treasury. In addition, the institutions may also be authorized to maintain accounts of the U.S. Treasury for the purpose of collecting receipts from Government agencies for credit to Treasury's account and for purposes of providing other services specifically authorized by the Secretary of the Treasury.

*Minority bank deposit program.*—Since Public Law 95-147 includes savings and loan associations in the class of financial institutions acceptable to become depositories and financial agents of the Government, the Banking Staff has been actively working to admit minorities' and women's savings and loan associations to the program. Staff action should be completed by early fiscal 1981, thus increasing the number of participants in the program by 80 percent. Through this program, the Treasury encourages Federal agencies, within the framework of efficient Federal cash management, to utilize eligible minorities' and women's financial institutions and disseminates information to those institutions to enable them to actively participate in supplying the Government's needs for various banking services.



*Federal depositary system.*—The types of depositary services provided and the number of depositaries for each of the authorized services as of September 30, 1979 and 1980, are shown in the following table:

Type of service provided by depositaries	1979	1980
Receive deposits from taxpayers and purchasers of public debt securities for credit in Treasury tax and loan accounts .....	14,079	14,117
Receive deposits from Government officers for credit in Treasury's general accounts..	715	706
Maintain checking accounts for Government disbursing officers and for quasi-public funds .....	5,572	4,425
Operate limited banking facilities in the United States and its trust territories .....	157	137

#### Operations planning and research

The Operations Planning and Research Staff continued its activities to improve a number of fiscal functions including the following major system revisions:

(1) In fiscal 1980 the Federal Reserve submitted all paid-check data for over 600 million checks to Treasury through the truncation system, a system whereby the flow of Treasury checks is stopped at the Federal Reserve bank level. Only payment data in the form of a microfilm and magnetic tape record is forwarded to Treasury for final payment and reconciliation processing. Processing times at the Federal Reserve banks were significantly reduced in fiscal 1980. New, more stringent processing goals had been set at the beginning of the fiscal year. Performance has been such that the previous goals were exceeded throughout fiscal 1980 with the new goals being achieved over 30 percent of the time.

(2) The direct deposit-electronic funds transfer program, through which recipients of recurring Federal payments receive credit directly in their accounts at their financial organizations, has been expanded to encompass almost 14 million payments a month. Approximately 139.3 million Treasury payments were made under the program during fiscal 1980. In 1980, virtually all of the program agencies are scheduled to have their salary payments brought into the program.

#### Miscellaneous fiscal activities

*Auditing.*—During fiscal 1980 a total of 94 audit reports on financial, compliance, and operational matters were issued. The audits ranged from small imprest funds to the accounting for multibillion-dollar Federal trust funds and the audit of U.S. Government-owned gold. In addition, 3 onsite examinations were made of the Bureau's disbursing centers throughout the United States and 37 onsite reviews of unfit-currency operations at Federal Reserve banks and branches.

Several auditors were assigned to special continuing projects that included: (1) Check payment and reconciliation task force, (2) payment processing system redesign task force, (3) claims modernization project staff, and (4) assistance to the Departmental Check Claims Oversight Group. In addition, staff members were assigned to special projects in the following areas: (1) Letter of credit operations, (2) Joint Financial Management Improvement Program, (3) Treasury tax and loan investment program, (4) Treasury financial communications system, (5) direct deposit/electronic funds transfer system, (6) Exchange Stabilization Fund audit, (7) investigation of fraud, (8) property management in BGFO, and (9) audit of the Treasury Historical Association.

As a result of the Audit Staff's annual examination of financial statements and related supporting information of surety companies, 306 companies

qualified for certificates of authority as acceptable sureties and reinsurers on bonds running in favor of the United States (6 U.S.C. 6-13). Certificates are renewable each July and a list of approved companies (Department Circular 570) is published annually for the information of Federal bond-approving officers and persons required to give bonds to the United States.

The Audit Staff also qualifies State insurance plans which provide insurance to cover Treasury tax and loan deposits in State-chartered credit unions and savings and loan associations (12 U.S.C. 266). The Staff devised the general standards for qualifying State insurance plans and four plans have been approved.

*Loans by the Treasury.*—The Bureau administers loan programs with those corporations and agencies that have authority to borrow from the Treasury. See the Statistical Appendix for table showing the status of those Treasury loans at September 30, 1980.

*Federal Financing Bank.*—During the period, loans outstanding were increased by \$18.3 billion, resulting in a balance at the end of fiscal 1980 of \$82.6 billion. Interest of \$6 billion was collected from borrowers and \$5.9 billion was paid on borrowings from the Secretary of the Treasury. See the Statistical Appendix for comparative financial data for the Federal Financing Bank.

*Liquidation of Postal Savings System.*—Effective July 1, 1967, pursuant to the Act of March 28, 1966 (39 U.S.C. 5225-5229), the unpaid deposits of the Postal Savings System were transferred to the Secretary of the Treasury for liquidation. As of June 30, 1970, a total of \$65.1 million, representing principal and accrued interest on deposits, had been transferred for payment of depositor accounts. All deposits are held in trust by the Secretary pending proper application for payment. Payments for fiscal 1980 totaled \$174,898. Cumulative payments amount to \$58.7 million plus pro rata payments to the States and other jurisdictions of \$6 million. The undistributed funds balance as of September 30, 1980, was \$206,968.

*Government losses in shipment.*—Claims totaling \$84,604 were paid from the fund established by the Government Losses in Shipment Act, as amended (40 U.S.C. 721-729). Details of operations under this act are shown in the Statistical Appendix.

*Donations and contributions.*—The Bureau received "conscience fund" contributions totaling \$98,751 and other unconditional donations totaling \$2,274,577. Other Government agencies received conscience fund contributions and unconditional donations amounting to \$27,240 and \$2,161,114, respectively. Conditional gifts to further the defense effort amounted to \$211. Gifts of money and the proceeds of real or personal property donated in this period for reducing the public debt amounted to \$830,662.

#### Foreign indebtedness

*World War I.*—The Governments of Greece and Hungary made payments during fiscal 1980 of \$83,424 and \$63,365, respectively. For a complete status of World War I indebtedness to the United States, see the Statistical Appendix.

*Credit to the United Kingdom.*—The Government of the United Kingdom made principal and interest payments of \$77.2 million and \$55 million, respectively, which were due on December 31, 1979, under the Financial Aid Agreement of December 6, 1945, as amended March 6, 1957.

*Lend-lease and surplus property.*—On July 1, 1980, the Government of France made the final payments under the lend-lease and surplus property agreements.

#### Payments of claims against foreign governments

The 20th installment of \$2 million was received from the Polish Government under the Agreement of July 16, 1960, and pro rata payments on each unpaid award were authorized. This payment fulfills the obligation of the Polish Government under the claims agreement.

The eighth and final payment of \$519,000 was received from the Hungarian Government fulfilling their obligation under the Claims Agreement of 1973. This pro rata payment has been authorized to all entitled awardholders, and payments are now being made.

A claims agreement between the People's Republic of China and the United States was concluded on May 11, 1979. Under the agreement, China will make six annual installments totaling \$80.5 million. The initial installment of \$30 million was received by the Department of the Treasury, and payments were made to entitled awardholders.

#### Administration

*Equal employment opportunity.*—In fiscal 1980, the Bureau exceeded its goal of 40 percent by filling 48.1 percent of available opportunities to hire and promote in grades GS-12 and above with minorities and women. The Bureau continues to make excellent progress in the resolution of EEO complaints. During fiscal 1980, eight complaints were filed at the Bureau. At yearend, only three of those remain to be adjudicated. The resolution of complaints prior to the hearing or court stages results in substantial financial savings in overall Bureau EEO discrimination complaint costs.

*Labor-management relations.*—On December 28, 1979, the Federal Labor Relations Authority (FLRA) certified seven BGFO disbursing centers as a residual unit represented by the National Treasury Employees Union (NTEU). A limited interim agreement was negotiated, and several issues were bargained to impasse. A Federal Services Impasses Panel decision on these issues was received August 27, 1980. Negotiations on the comprehensive field agreement were suspended in March 1980 because of severe staff shortages. However, these negotiations should reconvene in October 1980.

NTEU was active in fiscal 1980 in seeking to represent BGFO's three remaining disbursing centers within the contiguous United States. This effort was delayed pending FLRA General Counsel decision as to whether or not an election between NTEU and the American Federation of Government Employees (AFGE) may proceed. AFGE has represented the three disbursing centers in the recent past, and a joint BGFO/AFGE consolidation request was pending before the FLRA when the centers entered upon their respective open periods. While NTEU has submitted a petition to the FLRA showing employee interest, there is a legal question with respect to whether FLRA's pre-February 1980 regulations or their February 1980 regulations revision should apply in this case.

The BGFO headquarters unit of nonprofessional employees is represented by the NTEU. The final year of the first BGFO/NTEU 2-year contract ends in the fall of 1980, and negotiations on the second contract should begin in October 1980.

*Training.*—Four 3-day training sessions in employee relations for supervisory personnel were conducted in the Division of Check Claims. Training focused on questions and problem areas in labor and employee relations.

The "Careers in Management" course was conducted for all BGFO headquarters first-line supervisors. This course gives supervisors the tools to assess their skills, to develop an individual development plan for themselves, and to help their subordinates develop IDP's.



Executive and management development programs were developed and implemented. Eleven candidates were selected and are in various stages in their respective programs. Emphasis is on linking the upper and middle management programs and ensuring challenging developmental assignments to prepare candidates to successfully compete and, if selected, to perform well in managerial and executive positions.

A personnel intern program was implemented within the Personnel Administration Staff, and four candidates were selected to begin the program. Development was begun of a training package and appraisal system for merit pay for implementation in fiscal 1981.

The Career Development Program for Lower Level Employees (CADE) continues to be an effective means of selecting and training undertrained employees for higher level professional and paraprofessional positions. During fiscal 1980, 17 employees were selected and placed through this program.

*Procurement activity.*—The Bureau has continued to progress in meeting or exceeding its socioeconomic procurement program goals. More than \$1.1 million in contracts were awarded in fiscal 1980 to minority, women-owned, small business, or labor-surplus area concerns.

*Paperwork management activity.*—The largest compatible system of word processing equipment within the Bureau was made fully operational during fiscal 1980. Equipment for the system was installed in six locations within the Bureau for the use of organizations involved in the disbursement and claims processes.

A copy center was established in the Liberty Loan Building to support the activities of the Division of Check Claims. The preliminary cost benefit/feasibility study indicates that the system will provide cost savings of greater than \$26,500 over the next 5 years, and will relieve operating problems.

Recommendations resulting from two major micrographics studies for systems which would result in cost savings of over \$400,000 were approved by management during the year. One system, a source document application with in-house operation of microfilming, is already in limited use in the Division of Government Accounts and Reports. The other system, a computer output micrographics application, supported by a service bureau, which has application in the Divisions of Data Processing and Government Accounts and Reports, is nearly completed and soon will be fully implemented.

Additional maintenance support was secured from the contractor for the Division of Check Claims microfilm reader/printers and the Division's automated file retrieval system. Problems contributing to excessive downtime were identified, and corrective action was taken.

### **Bureau of the Public Debt**

The Bureau of the Public Debt is responsible for administering the laws and regulations pertaining to public debt financing and operations within the framework of policies established by the Secretary of the Treasury. The Bureau prepares regulations governing public debt securities, and the offering circulars and instructions relating to each offering of the securities; directs the handling of tenders or subscriptions and the making of allotments; supervises the public debt activities of fiscal agents and of agencies authorized to issue and pay savings bonds throughout the United States; orders, stores, and distributes all public debt securities; audits and records retired securities and

interest coupons; conducts transactions in public debt securities in Washington, D.C.; maintains individual accounts with owners of registered securities and book-entry securities and authorizes the issuance of checks in payment of interest and principal on such accounts; adjudicates claims on account of lost, stolen, destroyed, or mutilated securities; maintains accounting control over public debt financial and security transactions, security accountability, and interest cost; prepares public debt statements; and supervises the destruction of security items in the Department of the Treasury. The Bureau's principal office and headquarters is in Washington, D.C. An office is also maintained in Parkersburg, W. Va., where most Bureau operations related to U.S. savings bonds, U.S. savings notes, retirement plan bonds, and individual retirement bonds are handled.

#### Long-range planning (5 years)

Under the training guidance of the American Management Association, the Bureau Planning Team has developed 13 action plans that support 4 specific Bureau objectives. In June, the Executive Board reviewed and approved the first three of these action plans which address the following areas: Delegations of authority, performance awards, and classification of positions. Although these first three action plans are all in support of one objective—to increase the overall desirability of the Bureau as a Federal employer—they are representative of the long-range plan as a whole in the diversity of approaches being used toward the achievement of each of the Bureau's objectives.

#### Flexitime

In the first quarter of fiscal 1980, a feasibility study was conducted to determine if flexitime would improve productivity and employee morale. The determination was that flexitime plans should be implemented. Further studies performed in the second quarter developed policy recommendations. In the third quarter the Executive Board considered these recommendations and formulated a flexitime policy and plan which was approved. An agreement was negotiated with the bargaining unit. This modified flexitime plan was implemented in the fourth quarter. An evaluation of the flexitime plan has begun and will be completed in fiscal 1981. The results will determine whether or not flexitime will be continued.

#### Executive and management development

An executive development program for the Bureau was approved in March and plans were formulated for fiscal 1980 and 1981. On the basis of the plans, merit selection was completed by June 30, 1980, and one candidate was chosen for the Senior Executive Service.

The Bureau's Management Resources Board approved individual development plans for eight management candidates in March. The program (management development program) is being conducted by the American Management Association. In December 1979, the top management of the Bureau, including Division Directors, began a development program to enhance planning skills and improve planning processes. Additional candidates will be selected for the program.

#### Reorganization

In January 1980 the Office of Administration was established by merging the existing Division of Financial Management and Division of Management

and Support Services. The Office is responsible for Bureau-wide general management and administrative operations. This reorganization has resulted in a more responsive and effective administrative staff to support the operational components of the Bureau.

#### New series EE and HH bonds

The introduction of series EE and HH savings bonds between January and June 1980 and the discontinued sale of series E and H bonds required the development of new automated systems, forms, and procedures to maintain bond records, service inquiries, process claims, and account for the new bonds. The conversion to these new systems and procedures was accomplished in a timely and orderly manner.

Whereas the state of the economy has impacted sales, there are two changes in the terms and conditions of series EE bonds which produce savings and represent improvements under any condition. The first is a change of the minimum holding period from 2 months under series E to 6 months which has the effect of prorating the administrative costs over a longer period for those bonds redeemed within the first 6 months, thereby reducing the effective borrowing costs. The second is the elimination of the \$25 bond and changing the discount rate which effectively reduces the number of series EE versus E bonds sold for equivalent dollar amounts and reduces administrative costs which are based on bonds sold, serviced, and redeemed.

A monitoring process was established to assure compliance with the June 1980 issue date cutoff for series E bonds and with premature redemptions of series EE bonds. This surveillance will continue until the Bureau is reasonably certain that these terms and conditions are being met.

#### Treasury tax and loan investment program

Changes in the Treasury tax and loan investment program, authorized by Public Law 95-147, resulted in the formulation of the accelerated remittance system for savings bond sales proceeds.

Rules under which qualified savings bond issuing agents remit sales proceeds were amended in April 1979. This action was taken by Treasury to improve its cash management operations. Implementation of the rules was actively pursued during fiscal 1980, and over 80 percent of these funds are now being remitted timely. This represents a significant acceleration in the flow of funds to Treasury. In order to further improve system performance in light of this objective, modifications in two key areas were proposed and approved. From an internal standpoint, program and operational refinements were identified to streamline in-house accounting functions. The "policing" criteria of the system were also reevaluated to better identify noncomplying agents and improve the timeliness of their remittances.

#### Issues-on-tape (IOT) program

The IOT program provides high-volume agents an alternative to reporting U.S. savings bond issue transactions via registration stubs. This method of reporting is advantageous to the agents and to the Government both in efficiency of operation and cost-effectiveness. For every million registrations reported on magnetic tape, the Government realizes approximately \$20,000 in savings.

During fiscal 1980, 11 additional agents were accepted into the IOT program, bringing the total number to 88. Through July 1980, 48 percent of



total items reported and 54 percent of payroll sales were submitted on tape. While sales volume is down due to the state of the economy and introduction of the series EE bond, the IOT program continues to grow.

At current sales levels, the IOT program saves the Government approximately \$1 million annually. This savings results from the use of a less expensive bond assembly as well as reductions in manual processing, stub handling and storage, and shipping expense.

#### Interest on series E bonds/notes reported to IRS

The Bureau and the Internal Revenue Service have long been aware of the fact that much of the interest on series E bonds/notes is not reported as income by the individual taxpayer. In order to police the amount of such interest reported to the IRS, in July 1980 the Bureau began shipping, to eight IRS service centers, series E bonds/notes redeemed for cash since January 1, 1980. To date, approximately 114 million securities have been shipped to the IRS. The Division of Public Debt Accounting is charged with transferring liability for these items from the Savings Bond Operations Office to the IRS.

#### Bureau operations

During the fiscal year, 1,269,000 individual accounts covering publicly held registered and book-entry securities other than savings bonds, savings notes, individual retirement bonds, and retirement plan bonds were opened, and 1,001,000 were closed. This increased the number of open accounts to 1,171,000, covering registered and book-entry securities in the principal amount of \$22,395 million. There were 1,759,000 interest and discount checks with a value of \$4,224 million issued during that period.

Redeemed and canceled securities received for audit, other than savings bonds, savings notes, and retirement plan bonds, included 1,552,000 bearer securities and 604,000 registered securities. Coupons totaling 7,979,000 were received.

During the period, 38,000 registration stubs of retirement plan bonds, 25,000 registration stubs of individual retirement bonds, 41,000 retirement plan bonds, and 20,000 individual retirement bonds were received for audit and recordation.

*U.S. savings bonds.*—The issuance and retirement of savings bonds result in a heavy administrative burden for the Bureau of the Public Debt, including auditing and classifying all sales and redemptions; establishing and maintaining registration and status records for all bonds; servicing requests from bond owners and others for information; and adjudicating claims for lost, stolen, and destroyed bonds.

Detailed information on sales, accrued discount, and redemptions of savings bonds will be found in the Statistical Appendix.

There were 117 million registration stubs or records on magnetic tape and microfilm received, representing the issuance of series E and EE savings bonds, making a grand total of \$4,718 million, including reissues, received through September 30, 1980. All registration stubs of series E and EE bonds are microfilmed, audited, and destroyed, after required permanent record data are prepared by an EDP system in the Parkersburg office.

Of the 207 million series A-E/EE savings bonds and savings notes redeemed and charged to the Treasury during the period, 204 million (98.2 percent) were redeemed by authorized paying agents. For these redemptions the agents were reimbursed quarterly at the rate of 30 cents a bond, totaling \$61 million for the fiscal year.

Payment of fees to issuing agents was made at the rate of 5 cents for each book-entry reissue, 10 cents for each computerized payroll issue, 30 cents a piece for other payroll issues, and 70 cents for each over-the-counter issue. The issuing agent fees totaled \$18.1 million for the period.

Interest checks issued on current income-type savings bonds (series H and HH) during the period totaled 3,734,000 with a value of \$508.1 million. New accounts established for series H and HH bonds totaled 77,000 while accounts closed totaled 237,000.

Applications received during the period for the issue of duplicates of savings bonds and savings notes lost, stolen, or destroyed after receipt by registered owners or their agents totaled 58,500. In 32,000 of such cases the issuance of duplicate bonds was authorized. In addition, 16,000 applications for relief were received in cases where the original bonds were reported as not being received after having been mailed to registered owners or their agents.

## OFFICE OF FOREIGN ASSETS CONTROL

The Office of Foreign Assets Control administers five sets of regulations which implement the Department of the Treasury's freezing controls.

The Iranian Assets Control Regulations, issued by the Office on November 14, 1979, to be codified as 31 CFR part 535, block the property of the Government of Iran and its controlled agencies, instrumentalities, and entities, including the Central Bank of Iran. The regulations were issued pursuant to Executive Order 12170 of the same date, in light of the continuing crisis precipitated by the taking of the hostages at the American Embassy compound in Tehran, and the threat that Iran would summarily repudiate its obligations to American creditors and withdraw its assets from U.S. jurisdiction. The President declared a national emergency under the International Emergency Economic Powers Act, 50 U.S.C. 1701 et seq., the first use of that authority since its enactment in December 1977.

These regulations have been amended subsequently to implement further decisions by the President in connection with the crisis. On April 7, 1980, trade sanctions and further financial restrictions were imposed on Iran and its nationals pursuant to Executive Order 12205, and on April 17, 1980, travel restrictions and further financial restrictions were put into effect pursuant to Executive Order 12211.

In addition, on April 7, 1980, the Office issued reporting requirements implementing the President's decision to conduct a census of assets blocked on and since November 14, 1979, and a census of claims of U.S. nationals against Iran. The filing deadline for these reports was May 15, 1980, and, as of September 1980, the Office's Census Unit was completing the processing and computerization of data derived from approximately 1,100 assets reports submitted by over 300 holders of blocked Iranian assets and approximately 2,685 claims reports.

The Foreign Assets Control Regulations prohibit, unless licensed, all trade and financial transactions with North Korea, Vietnam, and Cambodia and their nationals. These regulations also block assets in the United States of the above-named countries and their nationals. The Cuban Assets Control

Regulations apply similar restrictions to transactions with Cuba and its nationals.

Until January 31, 1980, these regulations applied to the People's Republic of China and its nationals. However, under a general license in the Foreign Assets Control Regulations, all transactions with the People's Republic of China were authorized except transactions abroad by foreign firms owned or controlled by Americans which involved shipment to the People's Republic of China of internationally controlled strategic merchandise unless the transaction was appropriately licensed under the Transaction Control Regulations. Also, transactions in Chinese assets blocked in the United States as of May 6, 1971, remained prohibited until January 31, 1980, when the blocking regulations with respect to China were revoked.

Under the Agreement Concerning the Settlement of Claims between the Government of the United States and the Government of the People's Republic of China, signed on May 11, 1979, the People's Republic of China agreed to pay \$80.5 million in settlement of claims of U.S. nationals for expropriation of property from October 1, 1949, to May 11, 1979, and the United States agreed to unblock all assets remaining blocked under the Foreign Assets Control Regulations by reason of a direct or indirect interest of the People's Republic of China or nationals thereof. Regulations to implement the agreement were published January 31, 1980.

The Cuban Assets Control Regulations were amended on May 19, 1980, to add a section interpreting the prohibition of the regulations to apply to transactions in connection with the transportation of certain Cuban nationals to the United States (the "Cuban flotilla"). The regulations were again amended on August 24, 1980, to provide a general license for transactions incident to satellite telecommunications between the United States and Cuba for purposes of transmission of news coverage. The amendment also added a statement that specific licenses may be issued on a case-by-case basis for transactions incident to other communication activities.

The Transaction Control Regulations supplement the export controls exercised by the Department of Commerce over direct exports from the United States to Eastern Europe and the U.S.S.R. by controlling certain goods of foreign origin not subject to Commerce control. These regulations prohibit, unless licensed, the purchase or sale of strategic merchandise located outside the United States for ultimate delivery to Communist countries of Eastern Europe, the U.S.S.R., the People's Republic of China, North Korea, Vietnam, and Cambodia. The prohibitions apply not only to domestic American companies, but also to foreign firms owned or controlled by persons within the United States. A general license permits sales of these commodities to the listed countries (other than North Korea, Vietnam, and Cambodia) provided shipment is made from and licensed by a Coordinating Committee (COCOM) member country. (COCOM is a NATO entity.)

The Office also administers controls on assets remaining blocked under the World War II Foreign Funds Control Regulations. These controls continue to apply to blocked assets of Czechoslovakia, Estonia, Latvia, Lithuania, and East Germany and nationals thereof who were, on December 7, 1945, in Czechoslovakia, Estonia, Latvia, or Lithuania, or on December 31, 1946, in East Germany.

On September 8, 1980, the President made a determination that it is in the national interest of the United States to continue for another year, until September 14, 1981, the emergency authorities of section 5(b) of the Trading With the Enemy Act as a basis for the Foreign Assets Control Regulations,



the Transaction Control Regulations, the Cuban Assets Control Regulations, and the Foreign Funds Control Regulations.

On December 18, 1979, the Office amended the Rhodesian Sanctions Regulations by revoking all prohibition on transactions with Rhodesia. The regulations had been imposed pursuant to United Nations Resolutions calling upon member nations to impose mandatory sanctions on Southern Rhodesia. The amendment was issued to implement Executive Order 12183 of December 16, 1979, terminating limitations on trade and other transactions involving Zimbabwe-Rhodesia.

Under the Iranian Assets Control Regulations, the number of specific license applications received in the period November 14, 1979, through September 30, 1980, (including applications reopened) was 1,317. During this period, 1,124 applications were acted upon.

In fiscal 1980 the total number of applications for licenses received under the Foreign Assets Control Regulations and Transaction Control Regulations totaled 101, including applications reopened. The number that were acted on totaled 98.

Between October 1, 1979, and September 30, 1980, 555 applications were received under the Cuban Assets Control Regulations, and 529 were acted upon. In the same period, four applications under the Foreign Funds Control Regulations were received and a total of nine were acted on. Five were holdovers from the previous fiscal year.

Also in fiscal 1980, 179 applications were received under the Rhodesian Sanctions Regulations. A total of 366 applications were acted on, including 188 holdovers from the previous fiscal year.

Certain broad categories of transactions are authorized by general licenses set forth in the regulations, and such transactions may be engaged in by interested parties without the need for securing specific licenses.

During fiscal 1980, the Enforcement Section caused to be blocked, under the Iranian Assets Control Regulations and Cuban Assets Control Regulations, property in excess of \$10 million. Action taken by the Enforcement Section also resulted in the closing of a number of Iranian entities in the United States. One case, involving the transshipment of merchandise to Iran via West Germany, was referred to the Department of Justice for grand jury investigation.

## INTERNAL REVENUE SERVICE<sup>1</sup>

The Internal Revenue Service administers the internal revenue laws embodied in the Internal Revenue Code (26 U.S.C.) and certain other statutes, including the Employee Retirement Income Security Act of 1974.

### Collecting the Revenue

#### Returns received

The Internal Revenue Service received 143.4 million tax returns and supplemental documents during 1980, compared with 140.2 million in 1979.

<sup>1</sup> Additional information will be found in the separate Annual Report of the Commissioner of Internal Revenue.

Over 93.1 million were forms 1040 and 1040A, while 90.8 million had been received in the previous 12-month period. More than 37.6 million individual taxpayers—40.4 percent of all individual filers—used the form 1040A, compared with over 36.1 million in 1979. The number of individual taxpayers filing form 1040 increased to 55.3 million this year.

#### Mathematical correction

As a result of checking the mathematics on 88.9 million individual returns, 2.9 million taxpayers were found to have made mistakes that overstated their tax liabilities by \$591 million, an average of \$203 per return. On 3.6 million returns taxpayers had understated their tax liability by \$1.1 billion with an average of \$315.

Error rates for forms 1040 and 1040A rose slightly in 1980, with 6.3 percent of the 1040A's processed having mathematical errors, compared with 5.5 percent for 1979. The error rate for forms 1040 was 7.5 percent in 1980, 7.3 percent in 1979.

The IRS also checked the amounts claimed for estimated tax payments and found that taxpayers underclaimed \$618 million and overclaimed \$752 million.

#### Tax receipts

Gross tax receipts in 1980 rose to \$519.4 billion, passing the one-half trillion dollar mark for the first time. Total receipts showed an increase of \$59 billion—12.8 percent—over 1979.

Income taxes accounted for over two-thirds of all tax receipts. Individual income taxes of \$287.5 billion reflected an increase of \$36 billion, or 14.3 percent, over the prior year. Corporation income tax receipts were \$72.4 billion, an increase of \$932 million, or 1.3 percent.

Social security, self-employment, Federal unemployment, and railroad retirement taxes totaled \$128.3 billion, up \$15.5 billion, or 13.7 percent, from 1979. This rise reflects an increase in the social security tax rate from 12.1 to 12.26 percent on January 1, 1979, and an increase in the earnings base from \$17,700 in 1978 to \$22,900 in 1979 and to \$25,900 in 1980.

Excise tax revenue rose to \$24.6 billion, up \$5.6 billion, or 29.2 percent, over last year. The sharp increase—by far the largest ever recorded—was due primarily to the inflow of receipts from the new windfall profit tax.

Estate and gift taxes, the smallest source of revenue, advanced by \$1 billion—17.7 percent—to \$6.5 billion.

#### Refunds

The IRS paid \$54 billion in refunds to 75 million taxpayers including 4.5 million checks totaling \$1.3 billion for taxpayers who claimed the earned income credit. In 1979, 69 million refunds totaling \$41.7 billion were paid. Refunds to filers of forms 1040 and 1040A were \$44.4 billion, averaging \$614 compared with \$518 in 1979.

#### Penalties

Under law the IRS levies penalties such as those for failure to pay, paying with bad checks, filing late, or committing negligence and fraud. In 1980 the IRS assessed 20 million penalties for a total of \$2.1 billion.

### Tax credits

This year \$775 million in child-care credits, available to working parents meeting certain requirements, were claimed on 3.7 million returns.

Earned income credit (EIC) of \$2 billion was claimed by 7.1 million low-income taxpayers who maintain a home for themselves and at least one dependent. The Revenue Act of 1978 provided for advance payment of EIC in employee paychecks to give employees the option of receiving the credit amount each payday rather than waiting until the end of the tax year to get refunds from filing of individual income tax returns. Since the beginning of the program on July 1, 1979, \$26.1 million of advance EIC has been paid out by employers and reported on 39,300 employment tax returns.

Employers claimed \$582 million on 286,000 returns for the targeted-jobs credit in 1980. This credit replaced the new-jobs credit and is designed to encourage employment of specific groups.

This year taxpayers claimed \$478 million in credits on 4.8 million returns for energy conservation and renewable energy source expenditures made on their residences. This credit was provided by the Energy Tax Act of 1978.

Another tax credit of the Energy Tax Act of 1978 is the business energy investment tax credit (BEITC). The BEITC is refundable and can result in a refund in excess of tax liability based upon investments in solar and wind energy property placed in service between September 30, 1978, and December 31, 1979. This year taxpayers were allowed \$3.5 million to satisfy their current-year tax liability, and \$2.3 million in excess of their current-year tax liability.

### Presidential election campaign fund

This year 25.3 million individual income tax returns had designations for the Presidential election campaign fund—27.4 percent of the returns processed. Designations amounted to \$38.8 million compared with \$35.9 million designated in 1979 on 23.2 million individual tax returns, or 25.8 percent of those processed. The cumulative amount credited to the fund since 1972 is \$246.2 million.

### Combined annual wage reporting

Combined annual wage reporting (CAWR) is a system developed to reduce the reporting burden for employers while still satisfying the reporting requirements of both the IRS and the Social Security Administration (SSA). This reporting system became effective with all wages paid after December 31, 1977, for domestic employers and after December 31, 1978, for U.S. possession and Puerto Rican employers. Under CAWR, schedule A, which required a detailed listing of employee information, is no longer filed with employment tax forms 941, 942, or 943, and the form W-2 was redesigned to include the Federal Insurance Contributions Act (FICA) information formerly filed on schedule A. Forms W-2 are filed with the SSA, which processes the information and supplies it to the IRS.

During 1980, the IRS began a reconciliation between the employment tax returns such as forms 941 and 942 and the wage returns such as forms W-2 filed by employers for calendar year 1978 to insure that the correct tax has been paid over to the Government and that employees receive the correct FICA coverage with SSA.



### Windfall profit tax

The Crude Oil Windfall Profit Tax Act of 1980 imposed an excise tax on crude oil and certain natural gas liquids produced from domestic oil and gas wells after March 1, 1980.

Although the windfall profit tax is imposed upon the producer, the law provides that the first purchaser of domestic crude oil generally is liable for deducting and withholding tax from the purchase price, for depositing the tax, and for filing quarterly tax returns. This tax affects almost every taxpayer who owns any kind of an interest in an oil or gas well, including royalty owners, working interest owners and operators, as well as multinational oil companies.

Temporary regulations, dealing primarily with the administrative provisions of the law, were issued days after its enactment. Revenue rulings will be published, as necessary, to provide clarification, and one revenue ruling already has been issued involving the severance tax adjustment.

The amount reported for the windfall profit tax in 1980 was \$3.1 billion, and the first windfall tax examinations were begun in the fall of 1980.

A multifunctional IRS task force has been formed to identify problems and recommend solutions for the implementation of what is projected to be a 10-year program to collect \$227 billion enforcing this tax.

### Assisting the Taxpayer

This year the IRS received about 102,000 written, 35 million telephone, and 8 million walk-in inquiries from taxpayers requesting information about the tax system, their rights and obligations under it, and the tax benefits available. More than 59 percent of the inquiries occurred between January 1 and April 25, 1980: over 20 million phone calls, more than 5 million walk-in inquiries, and over 36,000 items of correspondence, totaling over 25 million requests for assistance. A quality check of 243,000 telephone responses and returns prepared by IRS assisters during this same period found an overall accuracy rate of over 97 percent.

#### Toll-free telephone assistance

Over 97 percent—19.8 million—of the telephone calls received during the 1980 tax return filing period were made through the toll-free telephone system that allows taxpayers from throughout the United States to call the IRS for information without paying long-distance charges.

Over 80 percent of these telephone calls are answered by frontline assisters. Referrals requiring computer research or more advanced technical assistance are resolved by IRS employees who have received specialized training in these areas. This year the IRS answered over 3.7 million account referrals, including inquiries on refunds, notices received, and tax payments. In addition, employees answered about 2.8 million technical referrals, responding to questions on corporation tax law, estate taxes, employment taxes, and a wide variety of other complex matters.

Teletypewriter equipment with a nationwide toll-free number giving hearing-impaired taxpayers access to telephone assistance was extended to Alaska, Hawaii, Puerto Rico, and the Virgin Islands.

#### Walk-in service

Walk-in taxpayer assistance was offered at inner city, business district, suburban, and rural locations with 702 permanent offices and 142 temporary offices set up especially for the filing period. In addition, over 37,000 banks

and Postal Service locations helped distribute more than 290 million tax forms and instructions.

The IRS provided foreign language assistance at 204 of its 844 taxpayer service offices. Spanish language assistance was offered at 154 of these offices by 600 employees, while 108 offices and 431 employees assisted in other languages.

#### Disaster assistance

In 1980 the IRS provided help in preparing amended returns and casualty loss claims and in getting refunds faster to taxpayers in 23 States and 138 counties affected by floods, hurricanes, tornadoes, and the eruption of Mount St. Helens.

#### Educating taxpayers

The "Understanding Taxes" and "Fundamentals of Tax Preparation" programs reached more than 5 million high school and college students last year. IRS-sponsored workshops for nearly 43,000 small business owners helped make taxpayers aware of their tax rights and responsibilities. In addition, 538 institutes were held for tax practitioners.

Through the volunteer income tax assistance program (VITA) the IRS recruits, trains, and supports volunteers who prepare tax returns for low-income, non-English-speaking, and military taxpayers. This year more than 355,000 Federal income tax returns were prepared by almost 55,000 volunteers. In 1980, as a result of a new program of tax counseling for the elderly, the IRS entered into agreements with nonprofit organizations to provide free tax help to individuals age 60 and over, with volunteers reimbursed for out-of-pocket expenses.

#### Forms and publications

The IRS contracted with an outside firm last year to revise and test the individual tax forms. Prototype forms have been developed and limited tests were conducted at various sites around the country. After the results of these tests are analyzed, large-scale testing with revised forms will begin early in 1981.

Public hearings held in Atlanta, Omaha, Seattle, and Burlington resulted in many suggestions on how to simplify the forms and instructions and after studying the suggestions the IRS has adopted a number of them. In addition, volunteers in San Francisco, Des Moines, and Jacksonville tested the form 1040 individual income tax returns and related schedules. The tests will assist the IRS in locating and modifying areas of particular difficulty on the forms. Computerized readability analyses also are being used to identify parts of the tax forms instructions that can be made easier to read.

The IRS distributed many taxpayer information publications free of charge including 2.8 million copies of Your Federal Income Tax, 1.4 million copies of the Tax Guide for Small Business, 805,000 copies of the Farmer's Tax Guide, and 71,500 copies of the Tax Guide for Commercial Fishermen. Additional tax materials were furnished to 7.1 million taxpayers, 580,000 tax practitioners, and 436,500 employers. The IRS publishes more than 90 booklets—3 in Spanish—on specific tax topics.

#### Informing taxpayers

Major television and radio networks and local broadcasters provided free air time having an estimated worth of \$5.5 million for this year's spot

announcements giving taxpayers information on provisions of the tax law and guidance on filing tax returns properly.

A new film, "A Right Good Thing," was produced to familiarize older Americans with tax counseling for the elderly and other available assistance in preparing income tax returns.

Specialized media receiving IRS information this year included newspapers and magazines read by farmers and fishermen, working parents, older Americans, barbers, beauticians, and service employees of hotels and restaurants. The information covered special tax responsibilities and benefits of particular interest to these taxpayer groups.

The IRS issued more than 7,000 news releases and responded to nearly 20,000 media inquiries through the National Office and 75 field locations.

#### Clarifying notices

In response to concern about the clarity of IRS computer-generated correspondence, a special effort began in July 1980 to review, revise, and reformat all such notices. The goal of this project is to make it easier for taxpayers to understand why they have received notices and what action, if any, they need to take in response. The IRS plans to begin using newly revised notices in January 1981. Taxpayer reaction to the notices will be tested, and feedback received will be used in considering future notice revisions.

#### Making information available

During 1979, the IRS processed 9,249 requests for IRS documents made under the Freedom of Information Act—an increase of 22 percent over 1978. Of this total 5,716 were granted in full, 1,097 were granted in part, and 2,436 were either incomplete requests or requests denied in full. The National Office reading room serviced approximately 31,000 additional requests for documents available to the public, including returns of exempt organizations, pension plans, and private letter rulings—a 17 percent increase over the prior year.

Under the Privacy Act of 1974, individuals made 371 requests for access to records about themselves and 20 requests to amend or correct these records. The IRS permitted full access in 185 of these requests and granted partial access in 82. The remaining 124 were either incomplete or denied in full.

Approximately 8,000 disclosures of tax information were made to the Department of Justice, 188,000 to Federal, State, and local child support enforcement agencies, and 71 million to State tax agencies under specific disclosure provisions in the Internal Revenue Code.

Effective June 1, 1980, authority for disclosure of tax returns and return information to Federal agencies for use in nontax criminal investigations was delegated to field offices to improve the timeliness of disclosure services.

The IRS has agreements with 94 State tax agencies for reciprocal exchange of confidential information. This Federal-State exchange program increases tax revenues, reduces duplicate examinations, and increases taxpayer compliance for both State tax agencies and the IRS. This year the IRS approved implementation agreements with 63 State tax agencies to identify more precisely the information to be exchanged and limit disclosures to information that is needed and used.

The IRS and the California Franchise Tax Board this year developed procedures that will eliminate duplicate paper processing of information returns filed. Each agency will transcribe a separate group of documents and exchange magnetic tape extracts. This cooperative effort will result in almost



100 percent transcription of information returns filed by California residents for use in document matching. The IRS is continually exploring methods of exchanging information by magnetic tape to improve utilization of State and Federal tax administration resources.

#### Helping other countries

In 1963 the IRS, in cooperation with the Agency for International Development (AID), initiated a program to assist foreign governments in modernizing their tax administration systems. During the past 17 years IRS advisers have been assigned to 38 countries, the Caribbean Community, and the Central American Secretariat for Economic Integration for periods from 2 weeks to several years.

In 1980 the IRS provided assistance to Egypt, Liberia, and Sierra Leone on long-term projects, while projects were completed in El Salvador, the Northern Mariana Islands, and the Trust Territories of the Pacific Islands. Short-term projects were conducted in Jordan and Trinidad and Tobago.

This year 405 officials from 74 countries visited the IRS for orientation and observation programs. Since 1963 over 5,750 visitors from 134 countries have participated in these programs.

This year the IRS also presented a 7-week INTAX seminar in tax administration for tax officials from six countries and provided a guest speaker at a seminar on computer-assisted audits sponsored by the Brazilian Ministry of Finance school.

#### Problem resolution

The problem resolution program (PRP) was established nationwide in 1977 to bring attention to taxpayer problems and complaints not promptly or properly resolved through normal procedures. In October 1979 the program was expanded to include all 10 IRS service centers.

Late in 1979 the IRS established a Taxpayer Ombudsman in the Office of the Commissioner to administer the nationwide problem resolution program, represent taxpayer interests and concerns within the IRS decisionmaking process, review IRS policies and procedures for possible adverse effects on taxpayers, propose ideas on tax administration that will benefit taxpayers, and represent taxpayer views in the design of tax forms and instructions.

The Taxpayer Ombudsman is not intended as a substitute for existing appeals procedures, nor is it meant to be another level of appeals, though advice on appeal rights is provided to taxpayers and complaints about appeals procedures are heard and acted upon by PRP offices.

This year 208,000 individual taxpayer problems were resolved through PRP. If a case cannot be resolved within 5 workdays, the taxpayer is contacted, advised of the status of the case, and provided the name and telephone number of the employee responsible for resolution. PRP also analyzes the underlying causes of taxpayer problems so that organizational, procedural, or systemic problems can be identified and corrected.

### Enforcing the Law

#### Examinations

During 1980 the IRS initiated a new method to group individual returns for examination selection purposes. Classes, which are groupings of returns by income levels, are used for scoring returns in the discriminant function system (DIF) (a computer method used to select individual returns for examination using mathematical formulas to measure the probability of error), planning

workload and staffing, and monitoring results of examinations. Total positive income (TPI), the sum of all positive income values appearing on a return, with losses treated as zero, now is being used to class nonbusiness returns, and total gross receipts (TGR), is used to group business returns. TPI replaces the previously used adjusted gross income (AGI) method of classifying returns.

#### Examination and correction results

The IRS examined 2,179,297 returns in 1980, of which 1,984,224 returns were examined in district offices by revenue agents and tax auditors—a decrease of 89,472 returns from 1979. The remaining 195,073 returns were examined in service centers, a decrease of 4,834 from 1979.

Revenue agents examined 615,671 returns at taxpayer residences or places of business—down 63,631 returns, or 9 percent, from last year. Tax auditors examined 1,368,553 returns using office audit procedures, down 25,841 returns, or 2 percent, from last year.

Examination coverage of income and estate and gift tax returns was 2.12 percent, compared with 2.24 percent in 1979.

The IRS examination program resulted in \$9.4 billion, the largest amount ever recommended in additional tax and penalties. Of this total, individual returns accounted for \$2 billion, corporate returns for \$6 billion, fiduciary returns for \$33.9 million, estate and gift tax returns for \$1.1 billion, and employment and excise returns for \$172 million.

The examination program also disclosed overassessments on 130,132 returns resulting in refunds of \$376 million, compared with 133,059 returns with refunds of \$328 million in 1979.

In addition to the district office examination program, service centers also resolve or verify issues that can be handled through correspondence with the taxpayer through a limited-contact correction program. During the year 533,046 returns were verified or corrected under this program and the information returns program (IRP). This figure is up 36,612 returns, or 7 percent, over 1979. Recommended additional tax and penalties totaled \$123 million, compared with \$119.2 million in 1979.

#### Large corporations

The coordinated examination program (CEP), which covers financial institutions and utilities whose gross assets exceed \$1 billion and other corporations whose gross assets exceed \$250 million, was restructured in 1980 to a two-tiered program and new case identification criteria were implemented. The two-tiered program involves a national CEP and a newly established regional CEP, with the most complicated cases assigned to the national program. The new, more sophisticated identification criteria consider factors such as asset size, multiple entities, multiple industries, complexities requiring specialists, gross receipts, and application of resources.

At the end of 1980, there were 937 cases in the national CEP and 567 cases in the regional CEP with a combined average number of open years per case of 2.8 compared to a 3-year objective. Recommended tax deficiencies and penalties totaled \$4.35 billion compared with \$2.7 billion for 1979.

In 1980 the industry specialization program included 13 designated industries, encompassing 483 of the national CEP cases.

In the computer-assisted audit program the IRS uses the skills of 174 specialists trained in computer systems hardware, program languages, and examination techniques to reduce the cost of investigations, examinations, and compliance projects. In the engineering program 12,459 referrals to engineer

agents for technical assistance were accepted—up 10 percent over last year. IRS has 319 field engineers located in 26 groups in 17 key districts.

#### Tax shelters

The tax shelter program was expanded and improved in 1980. At the end of the year 193,933 returns with tax shelter issues were in process, an increase of 11,202 returns over 1979.

A separate tax shelter staff was established in January 1980 in the Technical organization to accelerate the publication of rulings and furnishing of technical advice and assistance to IRS offices on tax shelter issues. During 1980, 13 tax shelter revenue rulings were issued and over 100 requests for technical advice and assistance from the Examination Division were processed.

Other improvements to the program include new procedures to identify abusive shelter cases—through information-gathering projects, utilization of information from other agencies, and greater use of “John Doe” summonses—and to expedite the appeals process.

With the addition of the commodities and real estate shelter areas this year, the tax shelter handbook developed for examiners now includes detailed examination techniques for seven of the most common shelters. Tax shelter training materials for examiners have been revised and updated and a separate course has been developed on commodities.

#### W-4 program

During 1980 the IRS developed a program to review and followup on questionable Forms W-4, Employee's Withholding Allowance Certificate, to check abuses by taxpayers who file incorrect W-4's with employers to avoid withholding of income tax from wages.

Amendments to the Employment Tax Regulations, issued March 11, 1980, require employers to submit certain forms W-4 to service centers, starting with their employment tax returns due in July 1980. If the IRS determines a form W-4 to be incorrect, the employee and employer will be notified that it is not acceptable. The employer then must withhold as if the employee were single, claiming no withholding allowances, until the employer receives a new form W-4 from the employee. Compliance with the new regulations will be monitored by district examination divisions during income and employment tax examinations.

#### Unreported income

The IRS is attempting to identify, examine, and investigate areas of high underreporting and nonreporting of income.

Beginning July 1980, a summary of information returns and currency transaction records filed for 1979 is being associated with 1979 individual income tax returns for use in the selection and examination of these returns.

Additional areas of potential noncompliance continue to be identified and tested to determine the extent of noncompliance.

#### Quality review

To assure impartial and uniform tax administration in resolving issues and making quality examinations, new standards and guidelines have been developed for selecting, examining, and reviewing returns. A system is also being designed to measure and report the quality of completed audits.



## Appeals

Under the single level of appeal begun in calendar 1978, and Revenue Procedure 78-9, the Appeals Division handled more cases than in prior years. Conferences were offered at all locations where previously held under the two-level system. In cases docketed with the U.S. Tax Court, 60 percent of appeals settlements occurred within 4 months and 88 percent within 6 months.

The number of cases received in Appeals continued to increase as more taxpayers exercised their appeal rights. Receipts increased from 48,845 cases last year to 53,467 cases during the current year. Docketed cases, those involving taxpayers who have filed petitions with the U.S. Tax Court, increased 7 percent and there was a 10 percent increase in nondocketed work. Small cases continue to be a large part of Appeals work with over 56 percent of receipts in 1980 involving cases with deficiencies of less than \$2,500, compared with 54 percent in 1979. Disposals also increased from 46,535 cases in 1979 to 49,971 in 1980.

The majority of cases handled in Appeals were settled with the taxpayer without the necessity of litigation. In nondocketed cases, 85 percent were closed by agreement, an increase from 82 percent, the revised agreement rate for 1979. In docketed cases, 61 percent were agreed in Appeals compared with 57 percent, as revised for 1979. The combined agreement rate for Appeals and district counsel, including those cases dismissed by the Tax Court, was 90 percent.

Ending inventory increased from 34,996 cases in 1979 to 36,047 at the end of this year. The potential tax liability represented by the cases in inventory increased from \$7.2 billion to \$8.7 billion.

A taxpayer whose informal request for abatement of certain penalty assessments is denied by service center or district office personnel may also request an Appeals conference. During 1980 Appeals disposed of 8,338 penalty appeals compared with 7,200 in 1979. Of the \$17.3 million in penalties protested, \$9.3 million was abated as a result of appeals.

## Criminal investigation

A total of 7,114 investigations were initiated in the general and special enforcement programs of the Criminal Investigation Division in 1980. The general enforcement program provides for balanced criminal tax enforcement involving various types of alleged violations of the tax laws and for geographical and occupational coverage of the population. Other enforcement efforts in this program include the prosecution of individuals who file multiple claims for tax refunds, illegally refuse to pay their taxes through various tax protests, and promote the use of fraudulent tax shelters.

In the special enforcement program individuals who derive income from certain illegal activities and violate the tax laws are identified and investigated. This program also includes projects such as the Federal strike force program against organized crime, the high-level narcotics financiers and traffickers project, wagering tax enforcement, and other efforts against racketeers.

Prosecutions were recommended in 2,267 investigations out of the 8,077 completed. Grand juries indicted or U.S. attorneys filed informations on 1,832 taxpayers. Prosecution was successfully completed in 1,601 cases.

Taxpayers entered guilty pleas in 1,244 cases, 93 pleaded nolo contendere, and 264 were convicted after trial. Acquittals and dismissals totaled 80 and 193, respectively. Of the 1,590 taxpayers sentenced during the year, 740, or 46.5 percent, received jail sentences.

Out of these totals, the special enforcement program accounted for 1,302 completed investigations, 455 prosecution recommendations, and 257 convictions or pleas of guilty to tax charges.

#### Cooperation with others

The Criminal Investigation Division participates in the Federal strike force program against organized crime. Strike forces are located in 13 major cities and are coordinated by Department of Justice attorneys. Investigations of high-level narcotics financiers and traffickers are coordinated with the Drug Enforcement Administration.

The Division also provides training in the use of financial investigative techniques against "white collar" crime to investigators for State crime commissions, U.S. probation officers, State securities commissions, U.S. Air Force Office of Special Investigations, State alcohol and beverage control divisions, State police, and other Federal, State, and local law enforcement agencies.

#### Illegal tax protesters

To address activities of illegal tax protesters, the IRS established a comprehensive program in January 1979 to identify illegal protest schemes and to take appropriate action through examination, criminal investigation, and collection programs to assure compliance with the tax laws.

As of June 30, 1980, over 9,000 illegal tax protester returns were under examination. During the first 9 months of 1980, 135 indictments or informations were returned on illegal tax protesters and 98 were convicted.

#### Collection

During 1980 the IRS disposed of 2.3 million delinquent accounts. Some \$6 billion in overdue taxes were collected. Of that sum, \$2 billion were collected in response to computer notices sent to taxpayers and \$4 billion were collected on delinquent accounts. Approximately 1.4 million delinquent returns were secured, involving \$1.8 billion in additional assessments. Returns compliance programs identified potential nonfilers and resulted in securing 55,469 returns with \$17.9 million in additional taxes assessed.

#### Service center collection

The service center collection function, which was developed and tested over several years, was operational in all centers during 1980. This function initiates correspondence and telephone contacts with taxpayers to resolve tax delinquencies and, under certain circumstances, makes arrangements with taxpayers to pay liabilities by installment. A collection activity reporting and evaluation system is measuring closely the efficiency and timeliness of service center collection actions.

#### Nonfiler identification

New procedures for early identification and contact of income tax nonfilers were implemented in 1980 and case selection criteria were refined to improve the quality of investigations and avoid contacts with persons not required to file. A study was completed to improve identification of nonfilers of business returns through matching information documents.

### Workload control

The IRS analyzed tax delinquencies during 1980 to identify measures to cope with increasing collection workload. For example, certain delinquencies were earmarked to receive additional notices and the timing between notices was changed to increase the possibility of collection before a field contact became necessary.

### Returns compliance

New returns compliance programs dealing with child care and agricultural labor were begun during 1980 after studies showed significant employment tax noncompliance in these areas.

The child care program resulted in several thousand investigations for nonfiling of Form 942, Employer's Quarterly Return for Household Employees, by taxpayers who listed large amounts for in-home child care on their income tax returns.

The agricultural labor program also resulted in several thousand investigations for nonfiling of Forms 943, Employer's Annual Tax Return for Agricultural Employees, by taxpayers who claimed large amounts for hired labor on Schedule F, Farm Income and Expenses.

### Bankruptcy

The Bankruptcy Reform Act of 1978, which became effective on October 1, 1979, had a substantial impact on the IRS collection operations. One of the most significant developments under the new law involves the special handling of tax returns. No tax may be assessed for periods ending before the bankruptcy proceeding began, until an automatic stay of assessment period has expired. To prevent assessment, a new computer program was designed to block the normal processing of tax returns from taxpayers who have declared bankruptcy. This allows the IRS to monitor the court proceeding and then assess the tax when legally permissible.

### Offers in compromise

The offer-in-compromise procedure, authorized since 1831 to compromise liabilities owed to the United States, is used as a tool to bring about maximum collection in situations where collection or the correctness of a liability is in doubt. The Collection Division processed 1,763 offers in compromise in 1980.

### Child support obligations

The law requires the IRS to collect delinquent child support payments on behalf of certain State agencies. In the past, IRS collection was used for cases in which a court-ordered child support obligation was delinquent and assignment of support rights had been extended as a condition of eligibility of aid to families with dependent children (AFDC). This year a change in the law extended the authority of the IRS to collect child support for non-AFDC families.

### Information returns program

In 1980 the IRS received over 358 million information returns from businesses and organizations reporting wages, interest, dividends, and other payments of which over 303 million were submitted on magnetic media. The Social Security Administration, which under combined annual wage reporting receives and processes forms W-2, received information from over 189 million forms W-2.



The IRS received over 100 million pre-1974 series E savings bonds redeemed in 1980 from the Bureau of the Public Debt for inclusion in the information returns program. These bonds date back to 1941. Since 1973, U.S. Government bond redemptions have been reported to the IRS on magnetic media.

The IRS will continue to match most information returns submitted on magnetic media against files to verify that correct amounts are reported on taxpayers' returns. Also, of the information returns submitted this year on paper, approximately 25 percent will be matched compared with 20 percent last year.

A new form, 1099 NEC, was provided this year for persons in a trade or business to report fees, commissions, or other compensation totaling more than \$600 for the year paid to anyone who is not an employee.

In 1980 the IRS notified over 2.1 million taxpayers of potential discrepancies between income reported on their tax returns and income reported on information returns. Also, 1.4 million taxpayers were sent notices of apparent failure to file tax returns based on information returns.

This year the IRS began using information returns in selecting returns for examination. Next year the IRS will use information documents in the collection program to locate and contact taxpayers who filed tax returns in previous years but failed to file tax returns for the current year.

#### International operations

To conduct the business of the IRS outside the territorial boundaries of the United States, the Office of International Operations (OIO) has foreign posts in key cities around the world. Because of the steady growth of the U.S. citizen population and business investments in foreign countries, this year the IRS increased the number of posts from 14 to 16, adding offices in Nassau and Vancouver. The Tehran post, which was closed in January 1979, was relocated in Jidda, Saudi Arabia.

Foreign posts are headed by revenue service representatives (RSR's) who manage the examination, collection, and taxpayer service programs at the posts in addition to conducting specialized investigations in support of U.S. domestic examination and criminal cases. Beyond this, RSR's serve as liaisons with foreign tax authorities in both treaty and nontreaty countries.

#### Compliance overseas

In 1980 over 16,000 returns were examined and nearly \$250 million in additional tax and penalties were recommended. About 10 percent of these returns were examined overseas. In October 1978 Congress enacted sweeping changes for the taxation of U.S. citizens working overseas. During this past year OIO examined the first returns filed since the change, and the effect of this legislation is being evaluated.

#### Assisting taxpayers abroad

For the 27th consecutive year the IRS provided tax assistance to taxpayers overseas with approximately 150,000 taxpayers visiting offices in over 120 cities in 68 countries. In addition, 84 tax seminars were attended by 1,800 taxpayers, and 7 military tax schools were held attracting over 550 participants who in turn helped thousands of service personnel overseas prepare their own tax returns.

### Tax treaties

The United States has income tax treaties with 40 countries and estate tax treaties with 13, designed to eliminate double taxation, remove tax barriers to trade and investment, and curb tax avoidance.

In 1980 OIO met with treaty partners throughout the world providing the framework for improved exchanges of information and for the resolution of double taxation cases. By exchanging information under the provisions of tax treaties, the IRS enhances worldwide compliance with U.S. tax laws, mitigates instances of double taxation, and assists U.S. businesses in securing uniform treatment of their international transactions.

OIO also continued to work closely with the Puerto Rican Department of Treasury and the Virgin Island's Department of Finance to resolve double taxation cases and to exchange taxpayer return information.

### Employee plans

A taxpayer compliance measurement program (TCMP) for employee benefit plan returns was started during 1980 to examine random samples of such returns to ensure continued compliance with the Employee Retirement Income Security Act of 1974 (ERISA). Data gathered during the examination of these returns will be used for planning future examination programs, improving the selection of returns for examination, and identifying needed changes to the series of forms 5500 returns and instructions. The program, which began in January 1980, will examine approximately 18,000 forms 5500 and 5500C returns with plan years beginning in 1978.

An ERISA noncompliance enforcement program was established this year to bring into compliance those employee benefit plans that received favorable pre- or post-ERISA determination letters but failed to comply timely with the law, final regulations, or other ERISA requirements. The program is designed to protect the rights and benefits of plan participants by providing limited relief from sanctions for those plans that voluntarily agree to comply with ERISA and restore any benefits to participants that were not provided because of failure to comply timely with ERISA.

A revenue procedure issued this year concerning simplified employee pension (SEP) plans gives guidance to sponsors seeking rulings and opinion letters for prototype SEP plans. SEP's, made possible by the Revenue Act of 1978, allow an employer to contribute annually up to the lesser of 15 percent of compensation, or \$7,500, to each participating employee's individual retirement account or annuity (IRA). A model SEP agreement (form 5305-SEP) available now is a qualified SEP with no further IRS approval when an adopting employer executes it properly.

A postreview program was initiated to ensure that all 17 key districts are uniformly applying the law and IRS procedures when issuing determination letters on the qualification of plans. Under this program, determination letters issued on the qualification of plans and the tax-exempt status of related trusts by key districts are subject to selection for post review by the National Office.

During the year 7 regulations and 32 revenue rulings and procedures were issued, as well as 4,621 National Office opinion letters, on master and prototype plans dealing with Keogh plans, corporate plans, and individual retirement accounts and annuities. In 1979 the IRS completed a review of pre-ERISA revenue rulings for modification, restatement, obsolescence, or revocation and during the current year began making public the results of this review.

Advance determination letters are issued by the IRS on the qualification of pension, profit-sharing, and other employee benefit plans. During the year 168,974 determination letters were issued on corporate and self-employed plans, an increase of 20 percent over 1979. Also, 19,378 plans were examined to determine the qualification of plans in operation, to verify the employers' allowable deduction for contributions to plans, and to assure that the rights and benefits of plan participants are protected.

#### Exempt organizations

During 1980, the Exempt Organizations activity issued or revised 8 regulations, 35 revenue rulings and procedures, 374 technical advice memorandums, 19 announcements, and 4 publications, and examined 23,807 exempt organization returns. In addition, 52,699 applications, reapplications, and requests for rulings from organizations were acted on.

A total of 22,582 organizations exempt under provisions of Internal Revenue Code sections 501(c)(3) through 501(c)(8) have been identified to be examined under the TCMP. Approximately 5,500 TCMP returns will be examined in each of the 4 fiscal years beginning October 1, 1980.

Examination guidelines were published to alert examiners to various private benefit or inurement schemes that may exist in the operation of home health care organizations. The examination coverage in this area increased from 5 to 10 percent in 1980.

The use of new guidelines that provide uniform procedures for identifying, investigating, and examining organizations employing questionable claims of tax-exempt church status have assisted in identifying such organizations and resulted in successful litigation against many.

On May 5 and June 6, 1980, the District Court for the District of Columbia in the *Green* case supplemented and modified a 1971 injunction prohibiting the IRS from recognizing racially discriminatory schools as tax-exempt under IRC 501(c)(3). Under the court order, the IRS is prohibited from recognizing the tax-exempt status of private schools in the State of Mississippi that have been adjudicated discriminatory, have been formed or expanded at the time of public school desegregation, and cannot demonstrate that they are not racially discriminatory.

The order further requires that the IRS survey all private schools in Mississippi to identify those that were created or expanded at the time of racial desegregation of the public schools. The IRS must then review facts and circumstances to determine if these schools discriminate in admissions, employment, scholarships, loan programs, athletics, and extracurricular programs. By terms of the order the IRS must report to the court in 6 months and then on each July 1 for the next 3 years.

The IRS is prohibited from following procedures similar to those required by the court order with regard to private schools outside of Mississippi. In these schools the IRS is applying the procedures and examination guidelines in effect before August 22, 1978.

### Managing the System

#### Research and operations analysis

During 1980 the IRS revised its long-range planning process to place greater emphasis on the analysis and executive assessment of critical issues and problems. The new process, including periodic executive issues conferences, a Service-wide research plan, and a strategic plan document, will be



phased in during 1981. Also, this year the IRS established a permanent unreported income research group.

#### Major research projects

Throughout 1980, IRS information-reporting programs were reviewed, a project was begun to measure compliance in reporting nonemployment compensation on the newly established form 1099-NEC, and a study continued on the feasibility of extending information reporting to bearer instruments.

Following a 2-year pilot study the IRS decided to phase in a program in which payers of nonwage income may satisfy both Federal and State information-reporting requirements by submitting a single magnetic tape of payments to the IRS that will, in turn, generate secondary tapes for State revenue agencies.

This year, as provided by the Revenue Act of 1978, the IRS began a study to simplify all individual income tax forms and instructions working with private design and language consultants. The study provides for a preliminary report to be sent to Congress in November 1980, while the IRS and the contractor will continue to test and refine the proposed new forms and instructions during 1981.

The IRS continued studies to determine compliance with some of the approximately 90 provisions in the Internal Revenue Code that allow taxpayers to defer certain tax consequences to later years. The tax return examination phases of several studies were completed during the year and the collected data are being analyzed to determine compliance levels, tax consequences, and the need for continued efforts in each area. These studies involve State income tax refunds, gains on sales of personal residences, and sales of stocks with cost basis reduced by splits or nontaxable distributions.

Other studies dealt with deferred gains on installment sales, amortization of changes in accounting methods, recapture of certain deductions on multifamily housing projects insured by the Department of Housing and Urban Development, and tracking amortization or depreciation on certified historic structures. Efforts also were begun to track certain other tax benefits such as the once-in-a-lifetime exclusion on gains from the sale of a principal residence and special farm valuations for estate tax purposes.

The IRS continued a study of the highway excise tax structure and different tax funding methods for the highway trust fund by sending questionnaires to IRS personnel engaged in the management, examination, and collection of taxes dedicated to this fund. Treasury delivered its first progress report on this study to Congress this year and the final report is due in April 1982.

#### Taxpayer compliance measurement

The taxpayer compliance measurement program (TCMP) is the basic IRS research activity for estimating the nature and extent of tax law compliance. The results are used to plan enforcement programs, improve computer selection of returns for examination, allocate IRS resources, formulate taxpayer information programs, and improve tax return forms and instructions.

This year the IRS completed TCMP examinations of a sample of corporation income tax returns filed in 1978 and started examination of randomly selected employee plan returns (forms 5500 and 5500C), individual returns (forms 1040 and 1040A), and exempt organization returns (form 990 series).

### Statistics

Statistics of Income (SOI) publications issued in 1980 included preliminary reports for individual tax returns for 1978 and unincorporated businesses for 1977, plus complete reports of individual returns for 1977, unincorporated businesses for 1976, and corporations for 1975.

The 1978 preliminary report for individuals contained statistics on the residential and business energy investment credits provided by the Energy Tax Act of 1978. Data reflecting the effect of other tax legislation as well as information on high-income taxpayers also were shown.

This year the IRS published its first supplemental report on domestic international sales corporations (DISC's), presenting information on products and services exported, by country for which the exports were destined. Two other supplemental reports provided information on the foreign income and taxes of U.S. corporations claiming a foreign tax credit and on the operations of foreign subsidiaries of U.S. corporations.

During the year the IRS also provided a report dealing with the sale or exchange of capital assets for tax year 1973, classified by type of asset, by the amount of adjusted gross income, and by the length of time the assets were held.

Other SOI publications completed in 1980 included a study of private foundations for 1974 and a report on individual retirement accounts for returns filed in 1976.

SOI publications may be obtained from the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402.

### Tax models

The five basic tax models—individuals, corporations, sole proprietorships, partnerships, and estates—used to make timely estimates of the potential impact and revenue effects of proposed tax legislation were updated in 1980. The models consist of computer programs to tabulate and analyze the most current SOI data available in these areas. Under a Federal-State exchange program State governments can obtain copies of the individual income tax model file for their tax administration purposes. The public may purchase from the National Archives the same file without data identifying taxpayers.

### Legislative analysis

This year the IRS developed 16 implementation plans to administer new tax legislation.

### Technical activities

During the year the IRS acted on 31,284 requests for technical advice, including 21,293 requests for changes in accounting methods and periods, and issued 456 revenue rulings and revenue procedures.

Letter rulings are written statements issued to taxpayers interpreting and applying tax law to specific sets of facts. Such rulings provide guidance concerning the tax effect of proposed transactions. Letter rulings are not precedents and should not be relied upon by taxpayers other than the recipient of the ruling.

Technical advice is issued by the National Office at the request of district offices to provide guidance on the proper application of the tax laws to specific facts in connection with audits of taxpayers' returns or claims for refund or credit.

A revenue ruling is an interpretation of the tax laws published in the weekly Internal Revenue Bulletin to inform and guide taxpayers, practitioners, and IRS personnel.

#### Updated procedures

During 1980 the IRS provided revised procedures for issuing rulings and determination letters and for entering into closing agreements, provided revised procedures for furnishing technical advice to District Directors and Chiefs of Appeals, and published a complete list of no-ruling areas that provides for early announcement of those issues added or deleted.

#### Internal Revenue Bulletin

The weekly Internal Revenue Bulletin announces official rulings and procedures of the IRS and published Treasury decisions, Executive orders, tax conventions, legislation, court decisions, and other items of general interest. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins. Weekly and semiannual issues are available to the public through the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402.

During 1980 the Bulletin included 398 revenue rulings, 58 revenue procedures, 15 public laws relating to internal revenue matters, and 19 committee reports, 80 Treasury decisions containing new or amended regulations, 19 delegation orders, 1 Treasury Department order, 22 notices of suspension and disbarment from practice before the IRS, 253 announcements of general interest, and 3 court decisions.

#### Art print panel

A new advisory group was created this year to advise the IRS on the valuation of lithographic prints. The art print panel consists of print publishers, distributors, retailers, and curators and will review taxpayer appraisals to determine whether claimed values can be supported. The panel will help the IRS cope with abusive tax shelters that use inflated appraisals of lithographic art print publishing ventures.

#### Internal audit

Additional revenue of \$150 million accrued to the IRS when management acted on internal audit reports that strengthened controls, improved operations, and brought about better service to taxpayers. Top managers were provided with a better perspective on how their functions operated through 42 coordinated audits that sampled offices to evaluate IRS programs nationally and regionally. Abstracts of internal audit findings are distributed monthly to IRS officials to alert them to areas that may need increased management attention. Reports are also made to top management on the implementation and effectiveness of actions taken on General Accounting Office reviews of IRS activities.

This year Internal Audit also established a group of auditors to review the design and development of new and significantly modified automatic data processing systems. These reviews determined whether internal controls, documentation standards, and audit trails existed and whether controls were cost effective, efficient, in compliance with legal requirements, and carrying out management policies prescribed for the system.



### Internal security

Internal Security Division investigations to protect the integrity of the IRS resulted in the arrest or indictment of 107 taxpayers and tax practitioners and 65 employees or former employees, and 89 persons were convicted or pleaded guilty. Of these convictions, 20 were for bribery and 14 were for assault while the rest involved conspiracy to defraud the Government, obstruction of justice, embezzlement, disclosure of confidential tax information, and impersonation of a Federal officer.

One investigation uncovered corruption involving members of an IRS unit that appraises values on real property. Bribes estimated at \$62,000 were paid to some IRS employees and a supervisor for placing low appraisal values on property for Federal estate and gift tax purposes. The appraisals were estimated at \$17 million below fair market value and the potential tax loss to the Government was approximately \$4.5 million. Former IRS employees, executives in private industry, attorneys, and certified public accountants were among the 13 defendants in this case. All were convicted.

Assaults and threats against IRS employees increased from 455 in 1979 to 508 in 1980. The Division protects all IRS employees so threatened or assaulted while performing their duties and seeks vigorous prosecution of these cases by U.S. attorneys.

In addition to investigating criminal misconduct or irregularities affecting IRS employees or operations, Internal Security conducts background investigations to determine the suitability of applicants and newly hired employees. The Division completed 11,727 background investigations of employees during the year and conducted police record checks on all persons considered for temporary appointments. These investigations and record searches resulted in the rejection of 107 job applicants and dismissals, suspensions, reprimands, warnings, or demotions against 376 employees. In addition, the Division conducted 527 investigations involving alleged employee misconduct and 128 of these investigations resulted in exoneration of the employees involved.

### Integrity program

Continuing its efforts to assist IRS managers in maintaining a high degree of employee honesty, the Inspection Service's integrity program is aimed at dealing with fraud, waste, and error before they occur. This program includes reviews and investigations to detect and deter material fraud and weaknesses in controls.

The Internal Security Division continued to increase the number of integrity awareness presentations to IRS employees, which include video tapes that realistically portray bribery situations as well as other possible integrity breaches employees may encounter.

### Fiscal management

During 1980 savings of about \$1.4 million were reported and verified through a management-generated savings program that rewards managers who cut costs. This procedure allows managers to reapply half of the savings resulting from their cost-cutting initiatives to programs under their control that they determine to be most in need of additional resources. The balance is used to deal with Service-wide problems or is given up in the next year's budget.

## Personnel

In implementing the Civil Service Reform Act, the IRS developed critical job elements and performance standards for managers and management officials covered under merit pay and implemented a Service-wide merit pay performance appraisal system. In addition, critical job elements and performance standards were established for approximately 55,000 employees under 300 different standard position descriptions not covered by merit pay. The Senior Executive Service and the Federal equal opportunity recruitment program were implemented, the Executive Resources Board was revised, a Performance Review Board was established, and all personnel training programs have been or are being revised to reflect new statutory and regulatory requirements.

## Awards and recognition

Joseph T. Davis, Assistant Commissioner for Resources Management, received the National Civil Service League Career Service Award this year. In September, Deputy Commissioner William E. Williams and Assistant Commissioner Davis were 2 of only 49 Federal executives to receive the SES Distinguished Rank Award from the President. In addition, four other IRS executives received SES Meritorious Rank Awards from the Secretary of the Treasury. They were: Thomas Cardoza, Western Regional Commissioner; William Waters, Mid-Atlantic Regional Commissioner; Americo Attorri, Mid-Atlantic Assistant Regional Commissioner for Resources Management; and Joseph Kump, National Office Fiscal Management Officer. Also, 56 employees received Presidential Letters of Commendation for contributions resulting in benefits of \$5,000 or more or for exceptional achievement in specific programs, and 49 more were recommended to receive commendation letters.

Awards presented under the IRS incentive awards program included 13 Commissioner's Awards, and nearly 13,000 awards to employees for adopted suggestions, sustained superior performance, and other special acts or services, saving about \$3.3 million.

## Facilities management

This year the IRS began a major building program in support of the service center replacement system that involves the replacement of almost all automatic data processing equipment in the 10 service centers. The design for the first group of five service centers was completed in 1980 and by 1983 new computer rooms will be finished in all centers.

An IRS/General Services Administration task force on energy conservation completed an onsite survey of all IRS service centers and established plans and schedules for immediate energy conservation. The measures recommended will result in energy savings of up to 33 percent based on 1975 use. This energy savings could keep approximately 3,600 average homes comfortable through one entire heating season.

Management's continued emphasis on reducing the number of calls placed over the Federal telecommunications system network enabled the IRS to absorb a tariff rate increase of approximately \$160,000 without additional cost.

## Training

This year a strategic plan for managing training in the 1980's was completed and adopted. As a result, about one-half of the training curriculum

in the next decade will be delivered at the larger posts-of-duty using computer-managed instruction rather than in centralized classrooms. This will result in a decreased need for instructors and a significant savings in travel and per diem.

The IRS also conducted a revised executive development program, added a new tax administration course to the executive training curriculum, and introduced a new computerized system for administering and monitoring individual development of executives.

A continuing professional education program was approved in May 1980 to provide IRS employees with training and work experience that will keep skills and knowledge current.

A new training program prepares internal revenue agents for the specialized role of summary or expert witness in trial appearances. Pretrial and during-trial duties and actual presentation of expert testimony are all stressed during the training.

Training also was developed to help problem resolution officers manage this new and growing program and to learn to identify systemic and procedural problems when attempting to resolve taxpayer complaints not satisfied through normal IRS channels.

In response to passage of the Crude Oil Windfall Profit Tax Act of 1980, training was developed to provide selected examiners with an understanding of the law and congressional intent, information about required examinations and verifications under the proposed regulations, and an overview of the reportwriting implications of the act.

Other new training programs developed in 1980 cover a basic and advanced statistical sampling course for revenue agents, combined annual wage reporting, disclosure orientation for service center employees, and illegal tax protester training for employees who have public contact.

And, the IRS has entered into an agreement with Arkansas Enterprises for the Blind so that some visually impaired students will receive IRS training needed for employment with the IRS.

#### Equal employment opportunity

From July 1979 to July 1980, full-time regular employment increased by 2.4 percent. The number of women employed increased 6.1 percent and minorities 12.6 percent. Women increased their representation in the higher grades from 5.3 percent of the positions at GS-13 and above to 6.5 percent and minorities from 6.5 percent to 7 percent. The employment of women and minorities also gained in such key jobs as revenue agent, attorney, criminal investigator, and appeals officer.

Nationwide, IRS offices observed such special events as Black History Month, Women-in-Government Month, Hispanic Heritage Week, and Asian/Pacific American Week. All managers and executives received equal employment opportunity (EEO) training as part of merit pay and SES training, while other EEO training was offered in courses such as that given to special emphasis coordinators.

IRS contract awards during 1980 totaled \$23,238,000 to small businesses and \$6,020,000 to minority and disadvantaged firms.

#### Data services

The past year has been a period of transition with Data Services preparing for the equipment replacement program (ERP). The Service and Design Division and the Systems Programming Division were merged to form a Tax Systems Division. Guidelines were established for systems development,



improved procedures were introduced for analysis, design, and programming, and greater emphasis is being placed on use of a high-level language for programming. In recruiting personnel to staff for ERP, special emphasis has been given to hiring minorities and women.

The service center replacement system (SCRS), the first portion of ERP, moved closer to realization with the issuance of a formal invitation to the computer industry to submit bids for the system. Another step toward SCRS was taken with nationwide installation of the data communications processing system (DCPS). DCPS currently augments the integrated data retrieval system and will be coupled with SCRS.

In 1980 Data Services worked with its IRS users to design and program changes that would eliminate the need at 10 service centers for manually sorting returns and documents by district office code. Beginning January 1, 1981, service centers will no longer sort most tax returns and related documents by the geographic locations in which taxpayers reside. Previously such sorting was done for control and accounting, but these procedures will now be automated. It is estimated that this refinement will save the IRS \$2.2 million when fully implemented.

Data Services also continued to respond to user needs for changes and improvements to existing programs. Currently there are more than 2,700 computer programs active in the National Office alone to meet user requirements.

#### National Computer Center

With construction and renovation continuing at the National Computer Center (NCC), five computer systems, the library of some 125,000 magnetic tapes and related functions, were moved to a permanent location in an addition to the existing building.

As of July the number of taxpayer accounts on the individual master file had grown to 117.2 million, an increase of 2.8 percent over the same period in 1979. The business master file grew to 22.9 million accounts—9.1 percent above 1979. The exempt organization, employee plans, and individual retirement account master files contain 1.1 million, 1.3 million, and 260,000 accounts, respectively.

A ninth computer system was installed and began producing in March, making it possible for NCC to respond to workloads such as the new system using data from more than 300 million information/wage documents to assist in screening returns for examination.

#### Detroit Data Center

The payroll system, which services all of IRS, was converted to a new computer system that now handles the biweekly payroll for more than 90,000 employees.

As the IRS central site for management information systems, the Data Center generates about 150 payroll reports and more than twice that many for other projects each month. And, this year the Data Center has provided TCMP tabulations, management information reports, and special evaluations such as the casino/racetrack winnings compliance study.

#### Chief Counsel

The Chief Counsel, an Assistant General Counsel of the Treasury Department, is the chief legal officer for the IRS and is a member of the Commissioner's executive staff. As such, the Chief Counsel advises the

Commissioner on matters pertaining to the administration and enforcement of the internal revenue laws and related statutes, as well as on nontax legal questions.

The Office of Chief Counsel employs over 900 attorneys, making it one of the largest law firms in the country. These attorneys are located in the National Office, the 7 regional counsel offices, and 45 district counsel offices.

Approximately 40 percent of attorney time is spent handling litigation in the U.S. Tax Court. The attorneys also advise the IRS and assist the Department of Justice on refund suits, criminal tax cases, suits seeking the disclosure of files and documents of the IRS, collection suits, and nontax litigation involving the IRS in Federal and State courts.

In 1980 the Chief Counsel library began to reclassify the 100,000-volume collection on taxation, legislation, and economics. The project will be accomplished with an automated cataloging system, allowing the library to participate in the Federal bibliographic data base, greatly expanding reference and interlibrary loan service.

#### Criminal tax

For 1980 there were 2,726 referrals by Counsel for prosecution and some 19,000 staff-hours were spent on legal assistance to Criminal Investigation Division.

Of interest to criminal tax enforcement this year is the Supreme Court decision in *United States v. Payner*, —U.S.—, 80-2 U.S.T.C. 9511 (1980), holding that the judiciary's supervisory powers do not permit the exclusion of evidence where the traditional tests of standing do not apply.

In *United States v. Carlson*, 617 F.2d 518 (9th Cir. 1980), petition for cert. filed (August 6, 1980, Docket No. 80-191), the court held that an individual cannot refuse to report income on a tax return on the asserted grounds that such reporting would be incriminating with respect to a prior tax violation.

#### Employee plans and exempt organizations

During 1980 the Employee Plans and Exempt Organizations Division developed regulations implementing the Employee Retirement Income Security Act of 1974 (ERISA), the Tax Reform Act of 1976, and the Revenue Act of 1978. Regulations were published in proposed, temporary, or final form on such matters as the limitations on contributions to and benefits from employee plans, the elapsed time rules for minimum vesting and participation requirements for employee plans, the rules for medical reimbursement plans, the rules for voluntary employee benefit plans, and the rules for disposition of private property and self-dealing for private foundations.

## BUREAU OF THE MINT<sup>1</sup>

The Mint became an operating bureau of the Department of the Treasury in 1873, pursuant to the Coinage Act of 1873 (31 U.S.C. 251). All U.S. coins are manufactured at Mint installations. The Bureau of the Mint distributes coins

<sup>1</sup> Additional information is contained in the separate Annual Report of the Director of the Mint.

to and among the Federal Reserve banks and branches, which in turn release them to commercial banks. In addition, the Mint maintains physical custody of Treasury stocks of gold and silver; handles various deposit transactions, including inter-Mint transfers of gold and silver bullion; and refines and processes gold and silver bullion.

During fiscal 1980, the first American arts gold medallions were produced and sold. The Mint performed the following functions on a reimbursable basis: The manufacture and sale of proof coin sets and uncirculated coin sets, medals of a national character, and, as scheduling permitted, the manufacture of foreign coins.

The headquarters of the Bureau of the Mint is located in Washington, D.C. The operations necessary for the conduct of Mint business are performed at seven field facilities. Mints are situated in Philadelphia, Pa., and Denver, Colo.; assay offices are in New York, N.Y., and San Francisco, Calif.;<sup>2</sup> and bullion depositories are located in Fort Knox, Ky., (for gold) and West Point, N.Y. (for silver).<sup>3</sup> The Old Mint, San Francisco, houses the Mint Data Center, the Mint Museum, and a numismatic order processing operation.

During the fiscal year, the Mint shipped approximately 16.3 billion coins to Federal Reserve banks, exceeding the alltime record of approximately 14.4 billion pieces set the previous year.

The Philadelphia Mint produced 6,190,322,000 coins; the Denver Mint, 6,661,831,227 coins; the West Point Bullion Depository, 1,591,000,000 coins; and the San Francisco Assay Office, 984,741,000 coins for general circulation.

The Bureau of the Mint deposited \$775,702,337 into the general fund of the Treasury during fiscal 1980. Seigniorage on U.S. coins accounted for \$662,714,791 of the total. The revenues deposited decreased about 25 percent from 1979, reflecting the decrease of approximately 33 percent in the amount earned from seigniorage. The decreased deposits are attributable to the decreased quantities of Susan B. Anthony dollar coins produced during the year.

#### **Domestic coinage**

The Mint manufactured, during the fiscal year, for general circulation, cupronickel clad dollars, half dollars, quarters, and dimes, cupronickel 5-cent coins, and 1-cent coins composed of 95 percent copper, 5 percent zinc. Production of the Anthony dollar was temporarily suspended at the end of March 1980.

With the purpose of assisting the public in distinguishing the Susan B. Anthony dollar coin from the quarter, the Mint conducted a study during fiscal 1980 to determine what changes could be made to the dollar to improve visual and tactile discrimination. The study concluded that the outer layers of the coin could be changed to brass-colored alloy consisting of 96 percent copper, 2.5 percent aluminum, and 1.5 percent silicon. The weight of the \$1 coin utilizing the new alloy would be 7.35 grams, compared with 8.1 grams. The study also determined that the reverse of the dollar coin could be changed to a design of a large Arabic numeral one with olive branch.

Improving the distinction of the dollar coin should result in wider acceptance of the coin by the public and increase its usage in commerce. To the extent that dollar coins are substituted for dollar notes, Government costs will be reduced.

A legislative proposal to change the composition, weight, and reverse design of the \$1 coin was prepared by the Mint prior to September 30, 1980.

<sup>2</sup> The San Francisco Assay Office also operates as a mint.

<sup>3</sup> Coinage operations are also performed at the West Point Bullion Depository.



During the fiscal year, the market price of copper briefly rose to the level at which the materials comprising the 1-cent coin nearly equaled its face value. As a result, the Mint conducted a comprehensive study to find a less expensive substitute material. The study updated an investigation of alternative materials for the 1-cent coin which had been prepared in 1974. Many different materials were studied for factors such as cost and availability, and were tested for wear, appearance, and coining characteristics. The study concluded that the present 95 percent copper, 5 percent zinc cent should be replaced by an alloy of 99.2 percent zinc, 0.8 percent copper, barrel electroplated with copper.

*U.S. coins manufactured, fiscal year 1980*

Denomination	General circulation		Numismatic <sup>1</sup>		Total coinage	
	Number of pieces	Face value	Number of pieces	Face value	Number of pieces	Face value
1 dollar:						
Cupronickel..	198,865,640	\$198,865,640.00	2,461,686	\$2,461,686.00	201,327,326	\$201,327,326.00
Silver-clad .....			196,544	196,544.00	196,544	196,544.00
50 cents:						
Cupronickel..	85,617,857	42,808,928.50	2,461,686	1,230,843.00	88,079,543	44,039,771.50
Silver-clad .....			196,544	98,272.00	196,544	98,272.00
25 cents:						
Cupronickel..	1,137,099,740	284,274,935.00	2,461,686	615,421.50	1,139,561,426	284,890,356.50
Silver-clad .....			196,544	49,136.00	196,544	49,136.00
10 cents.....	1,399,675,144	139,967,514.40	2,461,686	246,168.60	1,402,136,830	140,213,683.00
5 cents.....	929,255,632	46,462,781.60	2,461,686	123,084.30	931,717,318	46,585,865.90
1 cent.....	11,677,380,214	116,773,802.14	2,461,686	24,616.86	11,679,841,900	116,798,419.00
Total.....	15,427,894,227	829,153,601.64	15,359,748	5,045,772.26	15,443,253,975	834,199,373.90

<sup>1</sup> All numismatic coins were made at the U.S. Assay Office, San Francisco, and consisted of 1,892,407 1979 proof sets, 569,279 1980 proof sets, and 196,544 silver-clad Bicentennial sets (140,798 proof, 55,746 uncirculated). Production of Bicentennial coins ceased on Dec. 31, 1976; however, sets continued to be packaged and sold after that date. Bicentennial sets reported in this table were packaged and sold during fiscal 1980.

NOTE.—Dollars, half dollars, quarters, and dimes for general circulation and regular proof sets are three-layer composite coins—outer cladding 75 percent copper, 25 percent nickel, bonded to a core of pure copper. Dollars, half dollars, and quarters comprising the Bicentennial proof and uncirculated sets are three-layer composite coins with an outer cladding 800 parts silver, 200 parts copper, bonded to a core approximately 209 parts silver, 791 parts copper.

*Bureau of the Mint operations, fiscal years 1979 and 1980*

Selected items	Fiscal 1979	Fiscal 1980
Newly minted coins issued: <sup>1</sup>		
1 dollar.....	522,600,000	18,060,000
50 cents.....	101,700,000	111,922,856
25 cents.....	1,029,600,000	1,199,182,924
10 cents.....	1,227,400,000	1,391,906,790
5 cents.....	938,100,000	1,080,459,380
1 cent.....	10,543,700,000	12,511,901,500
Total.....	14,363,100,000	16,313,433,450
Inventories of coins in mints, end of period .....	2,492,500,000	1,607,600,000
Electrolytic refinery production:		
Gold—fine ounces.....	2,778,706.738	3,295,544.695
Silver—fine ounces .....	2,960,058.42	1,827,009.69
Balances in Mint, end of period:		
Gold bullion—fine ounces.....	254,538,826	251,700,922
Silver bullion—fine ounces .....	39,064,383	38,936,999

<sup>1</sup> For general circulation only.

The appearance of the 1-cent coins manufactured from copper-plated zinc would be nearly identical to the current cent; the weight would be 20 percent less. It is estimated that annual savings to the Government will exceed \$50

million. Based on these factors, the Mint has recommended conversion to the production of copper-plated zinc cents in phases over the next 2 years.

Beginning in January 1980, pursuant to a decision of the Director of the Mint, the "P" mint mark was placed on all denominations of coins manufactured at the Philadelphia Mint, except the 1-cent piece. Prior to 1979, when the "P" mint mark was placed on the Susan B. Anthony dollar, the "P" mint mark had been used only on the 5-cent coin produced during the World War II years of 1942-45.

Coinage strip for the manufacture of all denominations of coinage was provided from both in-house fabrication and purchased sources. The costs of in-house strip continued to compare favorably with those of purchased strip.

The Mint maintained its close liaison with the Federal Reserve System in determining coin requirements. Demand for coins, as measured by the net outflow from Federal Reserve banks to commercial banks, totaled 17.0 billion coins during the fiscal year. This represented an increase of approximately 24 percent from the previous year, attributable primarily to factors relating to the 1-cent coin. Speculation caused by increases in copper prices early in calendar 1980, as well as publicity about possible change in the alloy of the 1-cent coin, were considered major causes for increased demand for 1-cent coins.

The combined Mint/Federal Reserve inventories decreased from 5.7 billion coins on September 30, 1979, to 4.1 billion coins on September 30, 1980. The combined coin inventories at the fiscal yearend represents approximately a 12-week coin supply. Inventories of 1-cent coins decreased approximately 50 percent, from 2.9 billion coins at the end of fiscal 1979 to 1.5 billion coins at the 1980 fiscal yearend.

*Annual Assay Commission.*—The act of April 2, 1792, which established the United States Mint, also provided for the Annual Assay Commission. It is reported that the Assay Commission met almost every year from 1792 through 1980. Title II, Public Law 96-209, March 14, 1980,<sup>4</sup> abolished the Annual Assay Commission. The Mint at the present time produces no coinage utilizing precious metals.

#### Special coins and medals programs

*Foreign coinage.*—The Bureau of the Mint is authorized to produce coinage for foreign governments on a reimbursable basis provided that the manufacture of such coins does not affect U.S. coinage requirements. During the year, Mint installations manufactured 15,060,000 coins for the Dominican Republic and Panama.

*Proof and uncirculated coins.*—The Mint offered the 1980 proof coin sets for sale to the public starting on April 1, 1980, at \$10 per set. The sets, struck at the San Francisco Assay Office and bearing the "S" mint mark, contain one coin of each current denomination from the \$1 through the 1-cent coin. The ordering period was closed on May 9, 1980, after 3.5 million sets had been ordered. The first sets were mailed to customers in June. All sets were scheduled to be shipped by the end of December.

During the first quarter of the fiscal year, 2.6 million 1979 uncirculated coin sets were shipped to customers who had ordered them between September 4 and November 2, 1979. These 12-coin sets consisted of one coin of each denomination struck at each of the mints located in Philadelphia and Denver.

<sup>4</sup> See exhibit 35.

*Bicentennial coin sets.*—As reported in the 1979 Annual Report, the sale of the 40 percent silver-clad uncirculated Bicentennial sets was terminated in September 1979, when the open market price of silver reached a level at which the value of the silver in each set exceeded the price at which the Mint sold the sets. On December 17, 1979, the sale of the proof Bicentennial sets was terminated, when the open market price of silver continued to escalate. On August 4, 1980, sale was resumed of the 40 percent silver Bicentennial coin sets, at the price of \$20 per set for the proof and \$15 per set for the uncirculated. During fiscal 1980, 140,798 of the proof and 55,746 of the uncirculated Bicentennial sets were sold to the public.

*American arts gold medallions.*—During the fiscal year, the Mint struck the first 2 in the series of 10 gold medallions commemorating individuals specified as outstanding in American arts in Public Law 95-630, November 10, 1978.<sup>5</sup> The legislation provided that not less than 1 million troy ounces of fine gold be struck into medallions and sold to the public each year over a 5-year period. In 1980, 500,000 of the medallions honoring Grant Wood in the 1-ounce weight, and 1 million medallions honoring Marian Anderson in the half-ounce weight were manufactured at the West Point Bullion Depository.

The legislation authorized the medallions to be sold to the general public at a competitive price equal to the free market price of the gold contained therein, in addition to the cost of manufacture, including labor, materials, and use of machinery; and overhead expenses including marketing costs. The premium for each 1-ounce medallion was set at \$12 and the premium for the half-ounce was \$6. The Treasury offered the first 2 medallions for sale through the 35,000 post offices nationwide beginning on July 15, 1980. In the press release announcing the gold medallion sale, the Treasury indicated that the ordering period was expected to continue until September 30, 1980.

Between July 15 and September 30, 1980, the public ordered 183,000 of the Grant Wood medallions and 164,000 of those honoring Marian Anderson. Preliminary analysis of the sales indicates that the intent of Congress and the Department to achieve broad geographical distribution has been achieved.

*Medals.*—The gold medal in honor of John Wayne, authorized by Public Law 96-15, May 26, 1979,<sup>6</sup> was presented to the late actor's family in a ceremony at the U.S. Capitol on March 6, 1980. Bronze duplicates of the medal in two sizes were made available for purchase by the public. During the fiscal year, 51,000 of the 3-inch medals and 510,000 of the 1<sup>5</sup>/<sub>16</sub>-inch ones were manufactured and sold, making this the most popular medal ever offered by the Mint.

The gold medal authorized by Public Law 95-438, October 10, 1978,<sup>7</sup> honoring Lt. Gen. Ira Eaker, USAF (retired), was presented to the general on December 17, 1979.

Public Law 96-138, December 12, 1979,<sup>8</sup> authorized the President of the United States to present, in the name of Congress, a gold medal to the American Red Cross, in recognition of its service to the people of the United States. The design and engraving work on the medal was in process at the fiscal yearend.

On March 6, 1980, Public Law 96-201<sup>9</sup> authorized the President to present on behalf of Congress a gold medal to the Canadian Ambassador to Tehran, Kenneth Taylor, in recognition of his valiant efforts in securing the safe return of six American Embassy officials in Tehran. The dies and engraving

<sup>5</sup> See 1979 Annual Report, exhibit 24.

<sup>6</sup> See 1979 Annual Report, page 192 and exhibit 31.

<sup>7</sup> See 1979 Annual Report, exhibit 21.

<sup>8</sup> See exhibit 33.

<sup>9</sup> See exhibit 34.



work on the medal were completed and a trial medal had been struck by the fiscal yearend.

Public Law 96-211, enacted on March 17, 1980,<sup>10</sup> authorized the President of the United States to present on behalf of the Congress, to Simon Wiesenthal, a gold medal recognizing his contribution to international justice through documentation and location of war criminals from World War II. The obverse of the medal carries a portrait of Mr. Wiesenthal; the reverse features a torch superimposed on a world globe. The 3-inch gold medal was presented to Mr. Wiesenthal by President Carter in a ceremony in the East Room of the White House on August 5, 1980. Bronze duplicates of the medal may be purchased from Mint sales areas.

On July 8, 1980, Public Law 96-306 was enacted which authorized the striking of 650 gold-plated medals for those athletes selected through the Olympic trial process to represent the United States in the 1980 summer Olympics. The medals were intended to provide congressional recognition of the athletes' outstanding levels of excellence in their particular sports, since they were not permitted to compete at the XXII Olympiad in Moscow. The die work, engraving, and production of the medals were accomplished in record time. The medals were presented to the 1980 team members on the steps of the U.S. Capitol on July 30, 1980.

Trial strikes of the official medal for Secretary of the Treasury G. William Miller were awaiting the Secretary's approval at the fiscal yearend.

#### Gold refining and audit of gold holdings

The U.S. Assay Office at New York is the only Federal facility that refines gold and silver bullion. Refinery productivity was maintained and consolidated during the fiscal year. Unit costs, fine gold output, refinery positions, and gold anode inventory were essentially on target.

The Continuing Committee for the Audit of U.S.-Owned Gold stored at various depositories, with the responsibility to conduct audits at appropriate intervals, was established by the Fiscal Assistant Secretary of the Treasury during fiscal 1975. The Committee consists of one representative each from the Bureau of the Mint, the Bureau of Government Financial Operations, and the Federal Reserve Bank of New York, with General Accounting Office representatives invited to participate in the audits as observers. During fiscal 1980, gold audits were performed at three of the four Mint depositories where gold is stored: Fort Knox, Ky., U.S. Assay Office, New York, and the Denver Mint. By September 30, 1980, more than 64.2 percent of the U.S.-owned gold had been audited and verified. The continuing audit program is planned to provide a complete audit of all U.S.-owned gold by the end of the 10-year cycle in 1984.

#### Miscellaneous

The Bureau of the Mint continued the development of the financial management information system during fiscal 1980. The automated general ledger module was completed, with implementation scheduled for October 1, 1980. This system will interface with the automated obligation processing system implemented at the beginning of fiscal 1980.

The Mint's energy conservation program, designed to reduce consumption by 20 percent between 1978 and 1985, continued successfully. In fiscal 1980

<sup>10</sup> See exhibit 36.

energy usage was estimated to be 5 percent below that of 1979 and 8 percent below 1978.

During fiscal 1980, the Mint realized an 18-percent reduction in disabling illnesses and injuries.

The U.S. Secret Service surveyed all Mint production facilities and made a number of recommendations to improve security. The superintendents and officers in charge of the several Mint installations determined that the majority of the recommendations were feasible from a practical and cost perspective. An implementation plan was developed, and by the fiscal yearend more than 70 percent of the recommendations had been implemented.

During the fiscal year, the protection provided at the gold production and storage facilities was improved. At the West Point Bullion Depository a special security system, as well as complementary accountability procedures, was developed to protect the gold medallion program. Central to the system is an entry/exit procedure, consisting of an X-ray unit and a memory walk-through metal detector, which appreciably increases the probability of detecting thefts.

All Mint position sensitivity designations were revised and adjusted to conform with Treasury personnel security policies. In order to comply with Department document security requirements, 127 security clearances were reduced or administratively withdrawn.

Internal audits were made during the year of the processing and refining of Department of Defense silver-bearing scrap, and of travel expenditures at the U.S. Assay Office at New York. At the Denver Mint, the electronic surveillance and alarm systems, as well as the leave records, were audited. A review was made of the exhibits in the Mint Museum at the Old Mint, San Francisco. At the Philadelphia Mint the security functions were audited and an inventory was taken of special coins. A followup report was issued on the progress and problems of the Mint's numismatic sales areas. Credit card purchases at GSA self-service stores by Mint personnel were reviewed by the Internal Audit Staff. At the fiscal yearend, audit reviews of the following Bureau-wide activities were either in progress or in draft report form: (1) Building and Mechanical Divisions; (2) vault and safe security and weapons inventory; (3) appropriation accounting; (4) payroll; and (5) cash management activities. Audit reports on the numismatic coin operations system refunds and undeliverable coin sets at the Old Mint, San Francisco, were also being finalized.

The Internal Audit Staff assisted management in the development and implementation of the internal control system for the gold medallion program. It also periodically tested the adequacy of these procedures. In addition, the staff assisted Mint management in a review of the time expended on the annual settlements of the values held at each Mint facility. This included a survey of material handling systems at Mint installations and assistance in the preparation of the Settlement Task Force report for the Director of the Mint.

The Mint, through the facilities of its Laboratory in the Office of Technology, Washington, D.C., continued to provide technical expertise on the authenticity of U.S. coins. During the fiscal year, laboratory examination of 2,015 questioned coins relative to 167 cases was performed for the U.S. Secret Service. A member of the Mint's Technical Staff testified in four court cases pertaining to the authenticity of U.S. coins.

On February 15, 1980, an arbitration award was rendered on the grievances filed by AFGE Local 51, on behalf of 28 employees of the San Francisco

Assay Office. In the summer of 1979, these employees had been ordered by management to undergo fitness-for-duty examinations on the basis of their sick-leave records. After a hearing and submission of posthearing briefs, the arbitrator found that management did have just cause to order the medical examinations and, therefore, dismissed the grievances. On May 20, 1980, the Mint legal counsel submitted the Bureau's opposition to the exception filed by the union to the arbitration award dismissing the grievances of the employees. The decision on the matter was pending at the fiscal yearend.

The Mint improvement/expansion plan to expand coin production capacity and improve plant work environment was approved, but was not funded during fiscal 1980. If partial funding is approved in fiscal 1981, the funds will be used to expand and upgrade the Denver Mint.

## OFFICE OF REVENUE SHARING<sup>1</sup>

The Office of Revenue Sharing (ORS) is a part of the Office of the Assistant Secretary for Domestic Finance with a total staff of approximately 150 individuals. Offices are located at 2401 E Street, NW in Washington, D.C.

During fiscal 1980, \$6.8 billion in revenue sharing funds were distributed to more than 38,000 States, counties, cities, towns, townships, Indian tribes, and Alaskan native villages. This brought to \$55 billion the amount of money returned to State and local governments since the beginning of the general revenue sharing program in 1972.

The State and Local Fiscal Assistance Act of 1972 (31 U.S.C. 1221-1263) authorized the distribution of \$30.2 billion during the 5-year period that ended December 31, 1976. The money was allocated according to formulas contained in the law which use data on population, per capita income, and general tax effort for each recipient government.

The 11th entitlement period of the general revenue sharing program was the fourth and final entitlement period authorized by the State and Local Fiscal Assistance Amendments of 1976 (Public Law 94-488). These amendments extended general revenue sharing from January 1, 1977, through September 30, 1980, at higher annual levels of funding than had been previously authorized.

### Technical assistance

The Office of Revenue Sharing provides information and technical assistance to States and units of local governments receiving general revenue sharing funds.

Technical assistance was provided to recipients through more than 2,200 letters in response to written requests for specific information and guidance. Additionally, thousands of telephone contacts were made with local government officials, various organizations, and others interested in the revenue sharing program. Two technical factsheets pertaining to the changes in the auditing requirements of the program were substantially revised this year

<sup>1</sup> Additional information is contained in the separate Annual Report of the Office of Revenue Sharing.



with more than 50,000 individual mailings made of these and other informational materials.

The Office has broadened the network of liaison offices previously established within each of the 50 States. Sixty-eight technical assistance workshops were conducted during the year in cooperation with these liaisons and other cosponsors for the benefit of recipient governments.

An additional emphasis was placed on strengthening the effect of technical assistance to Indian tribes and Alaskan native villages during the year. Eight technical assistance workshops were held in conjunction with this effort.

Quarterly, each of the more than 38,000 recipient governments received a letter providing detailed information regarding the audit, public participation, reporting, and other compliance requirements of the program.

#### Data improvement

The accuracy of the individual data factors used in the computation of entitlements under the present distribution formula is a matter of significant concern to recipient governments. These data factors—population, per capita income, adjusted tax collections, and intergovernmental transfer revenues—are obtained from several sources, including the Bureau of the Census, the Bureau of Economic Analysis, the Bureau of Indian Affairs, and the Internal Revenue Service. The Office of Revenue Sharing has traditionally placed a high degree of emphasis upon efforts to ensure data accuracy.

The Office conducts, usually in mid-spring, a data improvement program whereby all eligible governments are advised of the individual data factors to be used in computing their allocations for the forthcoming entitlement period. Each government is asked to examine its data factors based upon established data definitions, and to propose corrections for any data elements believed to be in error. Typically, several thousand revisions may result from a single data improvement program.

Under normal circumstances, such a program would have taken place in the spring of 1980; however, because the program had not been reauthorized at that time, plans for a full-scale data improvement program for entitlement period 12 have been postponed.

Some important data improvement activities were, however, undertaken during fiscal 1980. The Office, in conjunction with the Bureau of the Census, sought to ensure that the data used to compute final 11th period entitlements in April 1980 were as comprehensive and as error-free as possible. At the beginning of fiscal 1980, approximately 2,000 governments had failed to provide essential data to the Bureau of the Census relating to adjusted taxes and intergovernmental transfer revenues despite collection attempts by that agency. With the Office of Revenue Sharing assuming responsibility for their collection at that point, reports were obtained from more than 1,200 previous nonrespondents in time for inclusion in the final 11th-period allocations. Challenges submitted in response to the 11th period's data improvement program were accepted through the end of fiscal 1980, as provided by statute. From the beginning of fiscal 1980, approximately 200 such challenges were received and acted upon by the Office.

In preparation for the general revenue sharing program's possible extension by Congress in essentially its present form, the Office obtained updated data for all four local government formula factors. (These consist of population estimates as of July 1, 1978; estimates of per capita income for calendar 1977, and adjusted taxes and intergovernmental transfer amounts relating to the local governmental fiscal year which ended between July 1, 1978, and June 30, 1979.) These data were subjected to rigorous analysis within the Office of

Revenue Sharing and the Bureau of the Census and are expected to be used in a data improvement program for entitlement period 12 should general revenue sharing be renewed.

The State and Local Fiscal Assistance Act of 1972, as amended, and regulations promulgated under title II of the Public Works Employment Act of 1976, as amended (antirecession fiscal assistance), require each State and local government which receives funds to supply information on its annual fiscal transactions, including data on the expenditure of funds received through either of these programs. A report has been published by the Bureau of the Census on data submitted by State and local governments entitled "Expenditures of General Revenue Sharing and Antirecession Fiscal Assistance Funds 1977-1978." It presents the data aggregated by type of government. In addition, individual government data are presented for all States, for the 63 largest counties, and for the 46 largest municipalities.

#### Data acquisition and analysis

The Office of Revenue Sharing evaluated the effects of proposed formula changes on the distribution of general revenue sharing funds. This information assisted the Department of the Treasury and the appropriate congressional committees in developing proposed changes in the General Revenue Sharing Act.

The Office began planning with the Bureau of the Census to obtain population estimates for Indian tribes and Alaskan native villages. The results of the 1980 census should permit the development of population counts for both.

#### Public participation

The public participation provisions of the Revenue Sharing Act require two public hearings by State and local governments receiving revenue sharing funds, prior to the use of such funds, with attendant public notice and opportunity for examination of budget documents and use reports.

Public participation compliance investigations were conducted in more than 175 recipient jurisdictions. Direction was provided to those governments which had failed to comply with public participation requirements to enable them to take voluntary corrective action.

Staff time and resources were allocated to "outreach" activities for the benefit of individual citizens and public interest organizations. Representatives of the Public Participation Compliance Branch participated in six national and/or local meetings of community organizations.

#### Auditing

The 1976 amendments to the Revenue Sharing Act require each recipient government receiving \$25,000 or more annually in revenue sharing entitlements to have an independent audit of its financial statements, in accordance with generally accepted auditing standards, at least once every 3 years to determine compliance with the act. This requires a financial audit of all funds and a compliance audit of revenue sharing and antirecession fiscal assistance funds. The audit requirements are applicable to nearly 11,000 of the 38,000 revenue sharing recipients.

During fiscal 1980, the Office continued its review of the professional practice of State auditors. Only 1 State audit agency out of 63 presently remains unacceptable, and it is anticipated that it can attain an acceptable status with very little additional effort. There are 63 State agencies because

some States have an agency for auditing State accounts and another agency for auditing local governments. The review of State agencies is a continuing program of the Audit Division.

The main thrust of the compliance effort during this fiscal year was the review of external audit reports; i.e., audit reports submitted directly to ORS by recipient governments. Where audits are performed or reports of independent public accountants are reviewed by a State audit agency, the agency provides ORS with a quarterly listing of the recipients covered during the period. Where items of noncompliance are noted, the agency provides ORS with copies of the report pages which show details of the violations.

During the fiscal year, 6,446 audit reports were received from local governments, of which 6,211 were acceptable. An additional 7,179 reports were received and reviewed for ORS by State auditors. There were 235 unacceptable reports submitted to either ORS or State auditors. At the end of the fiscal year, 1,209 partial reports had been accepted, but still required additional information to meet the requirements of the program.

In fiscal 1980, 150 noncompliance cases were opened, of which 137 resulted from findings of audit reports and 13 were the result of complaints. Cases closed totaled 175. Thus, open cases were reduced from 141 to 116, or a decrease of 25 during the year. As of September 30, 1980, there were only 17 cases that had been open for a year or more. At the end of the fiscal year, the total number of governments complying with the audit requirements was 6,956, or about 64 percent.

The Audit Division also responded to 4,207 requests from independent public accountants for confirmation of entitlement fund payments.

An automated audit tracking system installed during the previous year was modified to provide the number of recipient audit reports that have been received, whether they are acceptable, whether the audits were performed by State auditors, local government auditors, CPA's, or public accountants, and whether the financial statements are in conformity with generally accepted accounting principles or some other accounting basis. ORS notifies governments of their audit status.

#### Civil and human rights

Section 122 of the Revenue Sharing Act provides that: "No person in the United States shall, on the ground of race, color, national origin, or sex, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity of a State government or unit of local government, which government or unit receives funds \* \* \*. Any prohibition against discrimination on the basis of age under the Age Discrimination Act of 1975 or with respect to an otherwise qualified handicapped individual as provided \* \* \* shall also apply to any such program or activity. Any prohibition against discrimination on the basis of religion, or any exemption from such prohibition, as provided \* \* \* shall also apply to any such program or activity."

Although the Civil Rights Staff is small, it has investigated a significant number of complaints, many of which have been closed through negotiation and voluntary compliance. In those instances where recipient jurisdictions have been reluctant to take the necessary steps to comply with civil rights requirements, ORS has initiated action compelling them to do so.

Shown below is a table that demonstrates the growth of the activities of the Division.



*Discrimination complaints*

Year	Received	Determinations/ findings	Closed	Carried over
1972 .....	2	0	0	2
1973 .....	27	1	2	27
1974 .....	75	14	26	76
1975 .....	213	8	29	260
1976 .....	229	7	71	418
1977 .....	276	125	142	552
1978 .....	306	156	184	674
1979 .....	330	179	228	776
1980 .....	677	151	217	1,236

Note.—The most significant unit of work measurement is the determinations/findings issued, rather than number of complaints closed. The major portion of the work process is completed upon the issuance of a determination/finding. Usually, the closure of the case is dependent upon a review and analysis of requested information from a recipient government after the issuance of a noncompliance determination, or finding.

The Office continues to work in a cooperative effort with several Federal agencies to help resolve discrimination complaints and to assist in conducting field investigations. The Office is attempting to renegotiate cooperative agreements with the Federal agencies with which it has shared agreements. Agreements with the Office of Personnel Management and Law Enforcement Assistance Administration are currently in force.

A new Civil Rights Handbook was prepared to assist both recipient governments and the general public in understanding civil rights requirements of the program.

The basic technical memorandum relating to civil rights case processing was updated and improved during the year. Work on a comprehensive procedures manual for dealing with cases in which discrimination in the provision of public services is alleged is near completion. Using current personnel, a staff was established to monitor closed cases in which compliance agreements have been reached with jurisdictions.

### Systems Division

Standard letter formats oriented to word processing equipment were developed to streamline processing of the more common types of accounting correspondence. New procedures using these formats will provide more efficient use of the office staff and be more responsive in communicating critical information to the recipient governments.

Major revisions were made to the Accounting Manual, which documents the system of accounts and control procedures used to account for revenue sharing trust funds. The revisions strengthen internal financial controls and increase operational efficiency.

A computer system was implemented to calculate revenue sharing allocation adjustments. The system produces more accurate and timely adjustments to the recipient government accounts.

A large number of trial allocation distributions were produced using alternative formulas provided by congressional researchers and by the Office of State and Local Finance.

### Legal issues

In fiscal 1980 the Office of the Chief Counsel represented ORS in Federal court and at administrative hearings. It also negotiated and supervised compliance agreements settling compliance cases, drafted legislation and regulations, and provided legal counsel on a variety of issues.

ORS won a major legal battle on July 10, 1980, in *Board of Supervisors of Henrico County v. Blumenthal* (CA 79-1788), when the Fourth Circuit Court

of Appeals reversed a lower court ruling and held that the ORS procedure for computing adjusted taxes was lawful in that it was reasonably related to the purposes of the act. The court held that ORS was under no obligation to revise its bookkeeping system to make accommodations for individual recipient governments. The plaintiff filed a petition for a rehearing of the matter.

The Federal District Court of Connecticut ruled in favor of ORS when it denied the motion of the Middlebury Volunteer Fire Department to intervene in an administrative case involving sex discrimination against the town of Middlebury, *MVFD v. Peterson* (N80-134). The court also denied the MVFD's motion to enjoin ORS and the town from entering a compliance agreement. The case has been assigned to a U.S. magistrate for argument on the issue of a declaratory judgment.

The Chief Counsel's office continued to supervise a citywide compliance agreement with the city of San Francisco which arose from a suit alleging discrimination against Hispanic Americans.

The Office also prosecuted cases on the administrative hearing level, the majority of which concern civil rights violations under the act. In *ORS v. Borough of Haledon, N.J.*, the Director, for the first time, appealed an administrative law judge's finding to the Secretary of the Treasury. This appeal is still pending. The State of Alabama and several local governments were served with complaints alleging their failure to comply with the public participation and assurances requirements of the Revenue Sharing Act and regulations.

During this fiscal year, the Office of the Chief Counsel assumed responsibility for the procedure whereby jurisdictions which have been found by courts or administrative agencies to have illegally discriminated may have their revenue sharing funds suspended. The Office issued numerous notices of noncompliance and successful compliance agreements were attained in a majority of cases. Formal procedures for processing cases arising from judicial holdings were developed by the Director's office and the Office of the Chief Counsel.

Proposed regulations that included prohibitions against age and handicap discrimination as well as other regulations were published for comment during the fiscal year. A further revision of the regulations relative to nondiscrimination was forwarded to Health and Human Services, the Justice Department, and the Equal Employment Opportunity Commission for review. Proposed legislation to extend the revenue sharing program was also drafted.

## UNITED STATES CUSTOMS SERVICE

The U.S. Customs Service assesses, collects, and protects the levying of import duties and taxes; collects import and export statistics; enforces customs and related laws against contraband smuggling; controls carriers, persons, and articles entering or departing the United States by enforcing the Tariff Act of 1930 and other statutes and regulations governing international traffic and trade; and enforces the reporting requirements of the Bank Secrecy Act

by investigating financially motivated crime involving currency reporting violations.

To accomplish these missions designed to protect American trade and commerce and the safety of American citizens, Customs—

1. Acts as the principal border enforcement agency by enforcing more than 400 laws and regulations on behalf of more than 40 Government agencies to protect international traffic and trade.

2. Detects and prevents smuggling and other attempts to effect illicit entry into the United States of prohibited articles, narcotics, drugs, and other contraband.

3. Detects and investigates illegal activities to apprehend violators and effectively reduce, deter, and prevent violations of laws and regulations enforced by Customs.

4. Examines and clears carriers, persons, and merchandise to collect customs duties, taxes, fees, fines, and penalties in compliance with customs laws applying to international commerce.

During fiscal 1980, Customs collected \$8.2 billion in duty and taxes and processed \$180.4 billion worth of imports requiring over 4 million formal entries (those over \$250 in value). Some 47.5 million foreign mail parcels processed in fiscal 1980 required more than 2.2 million informal mail entries.

Customs cleared more than 297 million persons entering the United States, more than 89.6 million vehicles, 211,000 vessels, and 474,000 aircraft. This involved processing 17.1 million customs declarations.

Customs seized illicit drugs, prohibited articles, and undeclared merchandise valued at more than \$3.5 billion. The more than 21,595 drug seizures included: 4,742 pounds of cocaine, 43 million units of polydrugs, 2.3 million pounds of marijuana, and 268.7 pounds of heroin.

## Modernization

### Headquarters reorganization

The main objectives of the major reorganization of Customs' headquarters office, begun in 1979, were to structure a tightly knit policymaking organization at headquarters level, to achieve a more streamlined headquarters structure, and to reduce the size of headquarters. On April 6, 1980, the reorganization of Customs Service headquarters was completed. The new framework was designed to achieve a more balanced emphasis on both the commercial and enforcement components of the Service. The initial step was the establishment of four major offices: the Office of the Comptroller, the Office of Border Operations, the Office of Commercial Operations, and the Office of Management Integrity.

Realignment along these functional lines resulted in the placement of all enforcement-related organizations under the Office of Border Operations, and the consolidation of commercial functions under two suboffices, Regulations and Rulings and Trade Operations, in the Office of Commercial Operations. Streamlining techniques were applied throughout the reorganization process, as exemplified by the merger of all data systems responsibilities, previously existing as three separate organizations, into the new Office of Data Systems under the Comptroller. At the same time, the onboard strength of the headquarters work force was reduced through attrition by over 100 employees, and the ceiling was reduced by almost 200 positions through reallocation to field offices.



### Communications support

During fiscal 1980, Customs completed the installation of a communications network which provides substantially complete radio coverage around the perimeter of the continental United States. The network is controlled by eight regional communications centers.

Radio communications services were provided for the four ports of entry in the Alaskan Forty-Mile resource area, and for Anchorage.

Customs also completed a study of the feasibility and benefits of a single network capability to support the total data communications requirements of both Customs and the Immigration and Naturalization Service.

### Uniformity of procedures

Customs made significant progress towards its goal of establishing national uniform procedures during fiscal 1980.

An issuance established uniformity in entry acceptance. Also issued to field offices were uniform instructions on the processing steps to be taken to insure proper action in liquidating entries. Customs automated entry and accounting systems were programmed to allow direct online capabilities to extend or suspend an entry. This system, implemented in January 1980, proved successful in the application of Customs Procedural Reform Act provisions for liquidation.

To achieve uniformity in the application of Customs penalty laws relating to commercial violations, a legal monitoring program was established and tested during fiscal 1980. The program's purpose is to provide periodic legal review of actions taken in penalty matters by Customs field offices. Seminars conducted in each region informed concerned Customs personnel of correct procedures in penalty matters.

### Miscellaneous

During fiscal 1980, Treasury decisions published in the Federal Register relating to amendments to the Customs Regulations included the following:

T.D. 80-142, published May 1980, amended the Customs Regulations relating to imported petroleum and petroleum products to incorporate recommendations of the Customs Petroleum Imports Task Force. It established standard guidelines and procedures, including the use of public gaugers, to monitor imports of petroleum and petroleum products. These amendments should insure proper control of imported petroleum and petroleum products and uniform, complete, and reliable statistics relating to their importation.

T.D. 80-137, published May 1980, instituted a change of practice in the tariff classification of imported lightweight cab chassis. Treasury determined that the previous practice of classifying these chassis under the provision for bodies (including cabs) and chassis, in item 692.20, Tariff Schedules of the United States (TSUS), dutiable at the rate of 4 percent ad valorem, conflicted with principles announced in the decision of the U.S. Court of Customs and Patent Appeals in *Daisy-Heddon, Div., Victor Comptometer Corp. v. United States, C.A.D. 1228 (1789)*. As a result of this change, effective August 21, 1980, imported lightweight cab chassis are now classified under the provision for automobile trucks valued at \$1,000 or more in item 692.02, TSUS, dutiable at the rate of 25 percent ad valorem under item 945.69, TSUS.<sup>1</sup>

<sup>1</sup> See exhibit 42.

During fiscal 1980, Customs continued to publish its Customs Service Decisions (rulings), representing its official position on significant matters of widespread interest. These rulings were published in the Customs Bulletin to inform and guide the public, and in the Customs issuance system (CIS) for direct distribution to Customs field personnel. In the first 9 months of fiscal 1980, Customs published 297 decisions in the Customs Bulletin and 259 through the CIS.

## Trade

### Transfer of functions to Commerce

In compliance with the President's Reorganization Plan 3, the Trade Analysis Division under Customs' Office of Commercial Operations was transferred on January 2, 1980, to the International Trade Administration located in the Department of Commerce.

Antidumping, countervailing duty, and trigger price mechanism (TPM) functions formerly performed by Customs were incorporated into the new Commerce office. Customs remained responsible for collecting the estimated amount of antidumping and countervailing duties at the time of entry and liquidation of entries subject to these duties. Customs also retained responsibility for publishing information on antidumping findings in the Customs Regulations and for notifying the importing public of significant actions in antidumping and countervailing duty cases.

A liaison with the Department of Commerce, established by Customs, facilitated the smooth transfer of functions. During fiscal 1980, Customs developed the capability to provide Commerce with automated statistical data needed to conduct antidumping and countervailing duty investigations, and to insure that importers adhere to compliance agreements.

### Customs valuation

The new Customs Valuation Agreement incorporated in the Trade Agreements Act of 1979 became effective July 1, 1980. The agreement changed the methods used to determine the customs value of all merchandise imported into the United States.

### Tariff schedules

The Trade Agreements Act of 1979 resulted in more than 10,000 changes in such areas as rates of duty, Generalized System of Preferences (GSP) eligibility, nomenclature, quantity requirements, tariff item numbers, and Tariff Schedule headnote requirements. A new designation, least developed developing countries (LDDC), added to the tariff schedules during fiscal 1980, entitles certain products imported from LDDC countries to a rate of duty lower than the column 1 rate. All changes were implemented January 1, 1980, and relevant information was disseminated to the trade community in a timely fashion.

Other provisions of the Trade Agreements Act of 1979, effective during fiscal 1980, made significant changes in the duties and classification of benzoid chemicals, changed import requirements and quotas on cheese, established duty-free treatment of specialty beef from Canada, and repealed the wine-gallon method of determining distilled-spirit taxes.

The agreement establishes five bases, one primary and four secondary, for determining customs value. The bases are: First, transaction value of the imported merchandise (primary basis); second, transaction value of identical

merchandise; third, transaction value of similar merchandise; fourth, deductive value; and fifth, computed value.

If the customs officer cannot find a customs value under the transaction value, which is essentially the invoice price, the transaction value of the identical merchandise is used. If the value cannot be set from identical merchandise, the customs officer proceeds to the third method, and so forth down to the last computed value.

#### Miscellaneous

The Energy Policy and Conservation Act required the Department of Energy to establish standards for certain energy-using consumer products, and the Federal Trade Commission (FTC) to establish labeling requirements for the identified products. Importations of refrigerators, refrigerator-freezers, clothes dryers, water heaters, room air conditioners, and furnaces manufactured on or after May 19, 1980, must be labeled in conformity with FTC requirements. Customs issued appropriate field instructions during fiscal 1980, and began negotiations with both agencies to resolve key issues.

During fiscal 1980, the President continued the suspension of duty-free and license-free treatment of petroleum and petroleum products imports. Presidential Proclamation 4744 implemented a gasoline conservation fee and necessitated reissuing or changing import licenses. Further changes were mandated by court actions and the revoking by Congress of Presidential Proclamation 4744. Customs duties on petroleum and petroleum products were reestablished effective July 1, 1980.

The Civil Aircraft Agreement, effective January 1, 1980, stipulated the free rate of duty applicable to civil aircraft and parts and certification requirements.

### Merchandise Processing

#### Independent collection subsystem

With the consolidation of all Customs' commercial automation support under one program during fiscal 1980, the former automated merchandise processing system was supplanted by the independent collection subsystem (ICS), implemented by Customs nationwide. At present, ICS processes 100 percent of all collections at 73 Customs locations.

#### Automated broker interface system

Developed during fiscal 1980, the automated broker interface system is being tested in Baltimore and Philadelphia. The system accepts entry data electronically from participating brokers, thus reducing the need for Customs to keystroke entry documents for automated processing. A nationwide broker survey was conducted to determine the extent of broker automation and potential use of this interface system. In addition, separate broker and Customs evaluation teams were established to evaluate the pilot tests. Results will determine the approach for nationwide expansion of the system.

#### Selective examination of cargo

Customs evaluated its accelerated cargo clearance and entry processing test (ACCEPT) during fiscal 1980. This automated system communicates import specialist examination requirements to inspectors to assist in selecting and examining cargo for release. ACCEPT is predicated on the theory that not all cargo shipments or customs entries involve the same degree of risk, either for



regulatory and contraband purposes or classification and value. A revised version of this system will be field tested in New Orleans during the second and third quarters of fiscal 1981.

#### **Air cargo manifest system**

Customs air cargo manifest clearing system to automate clearance of air cargo manifests through online terminals continued to undergo testing with Flying Tiger Lines at Los Angeles International Airport. Meetings with other carriers were held during fiscal 1980 to determine their interest in participating in an east coast test of the system at JFK International Airport, New York.

#### **Import oil control**

During fiscal 1980, Customs amended its petroleum import regulations to provide for additional measurement controls and new requirements for public gaugers. To support these amendments, standard uniform operating procedures, technical measurement training courses, and a training manual were developed.

#### **Quotas**

One of the principal uses of vital trade statistics is to determine commodity quotas. Customs administers the various import quotas established by congressional legislation, Presidential proclamation, and directives from the Committee for the Implementation of Textile Agreements. In fiscal 1980, Customs administered 807 import quotas, including those applicable to textiles, meat, alloy tool steel, and color television sets.

The automated quota system, which became operational in fiscal 1979, was expanded by the addition of eight terminals in fiscal 1980. Quota terminal locations now total 35. In addition to determining quotas, Customs used it to administer import licenses issued by the Department of Agriculture. During fiscal 1980, Customs automated its processing of oil import licenses issued by the Department of Energy. This automated oil license system, a part of the quota system network, replaced a vessel manifest import reporting system instituted in fiscal 1979.

#### **Orderly marketing agreements (OMA's)**

OMA's are agreements whereby foreign countries voluntarily agree to restrict their exports to the United States. During fiscal 1980, Customs administered OMA's covering footwear, television sets, and meats. The OMA's with Japan, Korea, and Taiwan on color television exports, and with major meat-supplying countries expired during fiscal 1980.

#### **Import monitoring**

In addition to quotas and OMA's, Customs performs special monitoring of certain imports. Import monitoring information is used in international trade discussions and negotiations. During fiscal 1980, Customs monitored imports of certain textiles, meats, footwear, color television sets, and mushrooms.

#### **Regulatory audit**

The regulatory audit program is part of a broad-based Customs effort to modernize and simplify the processing of commercial transactions. The purpose of the program is to improve the revenue-producing function while protecting both the revenue and the importing public. Regulatory audit's

objective is to provide Customs with an external audit capability to verify transactions and claims of importers, carriers, and exporters. This is accomplished by means of onsite audits of their records, accounts, statements, and operating facilities in lieu of more costly physical control or other means of verification.

Field audits resulted in recovered revenues for the Treasury and importing public in excess of \$15 million as detailed below:

Type of audit	Number of audits	Amount recovered
Consumption entry.....	41	\$2,595,000
807.....	26	3,484,000
Drawback.....	239	2,907,000
Brokers.....	101	480,000
Other.....	80	5,919,000
Total.....	487	15,385,000

### Passenger Processing

To speed inspection of law-abiding travelers and facilitate detection of law violators, Customs relies on selectivity to identify those most likely to defy the law—companies as well as individuals. The primary tool in selectivity strategy is the Treasury enforcement communications system (TECS). An agreement with the Immigration and Naturalization Service and the Animal and Plant Health Inspection Service, implemented in 1978, led to the introduction of the one-stop system at selected international ports of entry. This system also facilitates passenger processing.

#### Treasury enforcement communications system

TECS is a computerized information and communications network which provides immediate information to aid customs officers in detecting violations of customs and related laws; enforcement figures to evaluate programs and performance; statistics to determine optimum allocation of equipment dollars and personnel; and data that Customs can analyze to produce intelligence on violation patterns, modus operandi, and courier profiles.

During fiscal 1980, installation of a new TECS passenger processing system was completed at all U.S. international airports. The system provides Customs with capabilities to: improve the overall quality of the TECS data base, notify originating offices when a subject of interest enters the United States and report the results of any enforcement actions, and improve displays at primary inspection stations to accelerate inspection. The new TECS system also provides for systematic collection of operational statistics to determine areas of the data base that require improvement, system utilization, and greater information effectiveness.

In fiscal 1980, TECS led to the seizure of more than \$200,000 in monetary instruments, more than \$750 worth of merchandise, more than 19 pounds of heroin, 140 tons of marijuana, 750 pounds of hashish, and 300,000 amphetamines. Alerted by TECS and the National Crime Information Center (NCIC) data incorporated into TECS, customs officers recovered 600 stolen vehicles and apprehended more than 1,300 fugitives wanted by other agencies.

#### One-stop

Under the one-stop system, all air passengers arriving in the United States bypass Immigration processing and proceed directly to the Customs area

after receiving their baggage. The inspectors from the different inspectional services are trained to perform certain primary functions for each agency.

One-stop was extended to airports serving Albuquerque, Atlanta, Houston, Los Angeles, and Denver. Customs is urging all airport managers to consider one-stop when constructing new facilities or renovating existing ones. Studies have shown that with accelerated airport baggage handling, Customs inspection can be speeded by as much as 20 percent.

#### Preclearance

The preclearance facility at Edmonton, Alberta, Canada, was opened in October 1979. Later in fiscal 1980, one-stop was extended to Edmonton. A total of 119,489 passengers passed through the Edmonton preclearance facility in fiscal 1980.

### Enforcement

#### Interdiction program

Customs tactical interdiction program combats smuggling activity along the national borders by reducing the smugglers' options for choosing the method, time, and place to attempt to enter contraband into the United States. This mobile interdiction force is capable of operations on land, sea, and in the air.

*Air interdiction.*—A fiscal 1980 interdisciplinary, indepth study of Customs' patrol air program addressed increased technical capability, mobility of response resources, optimum use of program resources, and detailed design of system elements which may be acquired, integrated, and operated to displace the air smuggling threat and support land and marine enforcement efforts.

During fiscal 1980, the air program resulted in the seizure of 50 vehicles, 95 aircraft, 8 vessels, 183,838 pounds of marijuana, 221 pounds of hashish, 723 pounds of cocaine, 4 pounds of heroin, 18 weapons, \$179,056 in monetary instruments, and \$601,448 in merchandise. A total of 222 arrests were made.

In June 1980, Customs accepted and put into operation its second Cessna Citation II fanjet aircraft equipped with modern, military-type radar and infrared sensors. In fiscal 1980, Customs also acquired and used an aerial photographic system developed by the Environmental Protection Agency. The system detects clandestine airstrips and unloading points used for air and marine smuggling.

*Land and marine interdiction.*—In July 1980, three unique, high-resolution search X-ray systems, built to Customs specifications, were installed at Miami and Dulles International Airports and at the Calexico port of entry. They provide maximum imaging of light-density materials like narcotics. The first of their type in domestic or foreign use, the systems will be used by Customs to examine suspicious items carried or worn by arriving air passengers and pedestrians crossing the border.

During fiscal 1980, Customs land program resulted in the seizure of 756 vehicles, 109 aircraft, 1,027 vessels, 1.8 million pounds of marijuana, 3,802 pounds of hashish, 1,798 pounds of cocaine, 127 pounds of heroin, 185 weapons, \$9,838,417 in monetary instruments, \$6,098,579 in merchandise, and 8,281 arrests.

The marine program effected the seizure of 50 vehicles, 2 aircraft, 95 vessels, 690,492 pounds of marijuana, 16 pounds of cocaine, 32 weapons, \$33,879 in monetary instruments, and \$63,834 in merchandise. Arrests totaled 286.



### Intelligence

During fiscal 1980, Customs adopted a centralized intelligence system to coordinate all of the intelligence information available inside and outside the Service. To this end, Customs intelligence requirements were reemphasized to members of the intelligence community through the National Narcotics Intelligence Consumer Committee, which includes the Drug Enforcement Administration, Department of State, and the U.S. Coast Guard. Nonnarcotics intelligence requirements were passed to appropriate agencies through bilateral meetings with the Defense Intelligence Agency and the intelligence components of the individual military services. Furthering its centralized concept, Customs issued an intelligence collection systems circular formalizing procedures by which intelligence requirements can be identified by potential collectors. A national system was established to measure the impact of intelligence data and products on enforcement results.

### Investigative activity

To identify those investigations that will result in significant seizures and arrests with national ramifications, Customs consolidated its 33 investigative categories into a more manageable 12-case system, and initiated an investigative case accountability system during fiscal 1980.

*Currency reporting violations.*—Because of the interrelationship between narcotics importation and the unreported transportation of currency out of the United States, Customs instituted Operation Money Project at 12 U.S. international airports. The purpose of the project was to generate actionable intelligence and interdict and/or document the outbound transportation of unreported narcotics-related currency in order to develop felony currency conspiracy cases. Customs continued to emphasize the importance of intelligence research and cooperation with other agencies in uncovering currency transportation reporting violations. "Cash flow" investigative units were expanded to Houston, Dallas, San Diego, San Francisco, Chicago, Boston, New York, and Baltimore. In addition, a joint Customs/Treasury financial investigation was initiated in Florida.

*Fraud.*—In support of its ongoing effort to deny criminal elements the financial benefits generated by their illicit activities, Customs completed 11 intelligence analyses that identified 440 individuals and 66 businesses suspected of the movement of at least \$436.5 million. Formats for the use of the financial information files to identify persons, firms, and financial institutions suspected of illicit or improper activities were designed and implemented.

### Terrorist contingency planning

During fiscal 1980, Customs participated with other agencies in long-range planning and preparation for the Lake Placid Winter Olympics. Antiterrorist training was conducted at all the Olympic ports in conjunction with other Government agencies. Customs provided 45 TECS terminals for its own use and that of Immigration and Naturalization and other Federal enforcement agencies. The screening system used by Customs to support land border and airport inspections was placed in use at Lake Placid and served command post operations coordinating Federal, State, and local activities. Customs also constructed special facilities and solicited Federal and local law enforcement cooperation to accelerate passage of arriving persons and equipment.

**Monitoring of in-bond cargo**

To determine whether the Customs in-bond cargo system was being used for smuggling, Customs conducted a tracking test of in-bond air cargo between New York and Dallas/Ft. Worth and Chicago and San Francisco airports. Several seizures were made.

**Miscellaneous**

To implement new metric standards of fill and labeling requirements for imported alcoholic beverages, effective January 1, 1980, Customs engaged in extensive programs with the Bureau of Alcohol, Tobacco and Firearms and the responsible international communities to detect and monitor fraudulent labeling and certificates of origin.

**International Matters****Saudi Arabian assistance project**

The objectives of the U.S. Customs Service Saudi Arabian technical assistance programs are to modernize and improve the efficiency of the Saudi customs service. To support these objectives, U.S. Customs is establishing an Office of Saudi Arabian Programs under the Deputy Commissioner to centralize and promote the priority of such highly technical programs as data processing, micrographics, contraband sensing, and management and computer training.

**Customs Cooperation Council**

U.S. Customs active participation in the Customs Cooperation Council (CCC), an 88-member intergovernmental body with headquarters in Brussels, contributed to a number of advancements of benefit to the international community.

During fiscal 1980, the Council adopted four new technical annexes to the International Convention on the Simplification and Harmonization of Customs Procedures, bringing the total number of annexes adopted to 30 and completing the Convention.

Work continued on development by the CCC of a harmonized commodity description and coding system of importance to both U.S. Government agencies and private industry. Through its chairmanship of the Interagency Committee on Customs Cooperation Council Matters, U.S. Customs helped the CCC advance toward this goal.

The Council sponsored meetings of an Interim Technical Committee to consider administration of the new General Agreement on Tariffs and Trade (GATT) valuation code. A U.S. customs officer was elected Director of the Valuation Committee.

**TIR Convention**

In July 1980, Customs recommended accession of the United States to the 1975 Customs Convention on the International Transport of Goods under cover of TIR Carnets (TIR Convention) in testimony before the Senate Foreign Relations Committee. The Convention was favorably reported out of the committee to the Senate for advice and consent to ratification.

**International training activities**

During fiscal 1980, approximately 460 foreign customs officers attended narcotics enforcement courses conducted by U.S. Customs in Peru, Turkey,

Pakistan, the Philippines, and the Caribbean area. Training programs for foreign customs personnel conducted by U.S. Customs in the United States included 2 midmanagement seminars at Customs headquarters attended by 39 representatives of Latin America and Southeast Asia, areas of intense narcotics activity. A 3-week dog trainer/administrator course and a 12-week detector dog handler course were conducted by Customs at its Detector Dog Training Center near Front Royal, Va.

#### Miscellaneous

Customs implemented the Foreign Assets Control prohibition, effective April 7, 1980, on most exports to Iran. This was followed by an import prohibition effective April 18.

The easing of tensions in Rhodesia prompted the removal, on December 16, 1979, of Rhodesian sanctions enforced by Customs for many years.

Customs enforces the prohibition required under the Fishery Management and Conservation Act against the involved country and fishery whenever American fishing vessels are seized. Prohibitions were placed on tuna and tunafish products from Mexico, Peru, Costa Rica, and Canada as a result of adverse actions against American fishing vessels. However, later in fiscal 1980 prohibitions were lifted for Costa Rica, Canada, and Peru.

The Marine Mammal Protection Act requires a prohibition against the involved country and fishery not conforming to the act. During fiscal 1980, Customs enforced prohibitions against the importation of yellowfin tuna and tuna products from Senegal, the People's Republic of the Congo, and Peru.

### Management

#### Equal opportunity

A major functional, organizational, and position classification review of regional equal opportunity operations was conducted by Customs to increase the effectiveness of its equal opportunity programs in the field. The Federal Equal Opportunity Recruitment Program Conference held at Customs headquarters during fiscal 1980 established, as a national objective, creation of a data base system to gather minority statistics.

#### Economic analysis support

Customs Office of Economic Analysis (OEA) completed numerous economic/planning studies, projections, and analyses on a wide variety of issues during fiscal 1980.

Profiles and projections were prepared for every Customs port, and development of a Customs data bank was initiated to provide Customs and other Treasury officials with immediate access to up-to-the-minute data on Customs workload and on international trade.

Economic and regulatory analyses conducted by OEA during fiscal 1980 covered such issues as foreign trade zones, antidumping and countervailing duty cases, cargo/entry processing selectivity, the U.S. television receiver industry, economic conditions in Mexico and their effect on the United States, duty collections from the People's Republic of China, the cost of implementing the proposed Regulatory Cost Accounting Act, and the cost of requiring earlier payment of customs duties. OEA also conducted studies on international trade and travel trends, and provided weekly reports for Customs officials on significant international economic developments.



### Data processing

An automated data processing security program established during fiscal 1980 protects the integrity of Customs ADP installations and programs by developing, monitoring, and evaluating ADP systems security.

The Customs appropriation management information system was developed and tested in Baltimore and Washington, D.C., during fiscal 1980. The new automated appropriation accounting system will become operational nationwide in fiscal 1981.

### Management information systems

Customs management information systems were extended during 1980 to include the CF-16 transactions reporting system which provides a Customs workload count by geographical location and helps determine resource allocations; the report of Customs workload and service performance which analyses workload fluctuations; the report of monthly operating statistics, a statistical comparison of regional performance data relevant to workload, resources, enforcement, and general performance indicators; and the report of Customs efforts, a comparison of regional management activities which provides top management with a basis for determining overall management performance and identified matters requiring management attention.

### Program evaluation

During fiscal 1980, the Program Evaluation Division, formerly the Management Analysis Division, completed four major program evaluations at the direction of the Customs executive staff. These evaluations included the following:

*Detector dog program.*—The purpose of the review was to evaluate the overall effectiveness of the program in meeting its objectives; describe the program as it was operating; identify program variables; and recommend to management adjustments which could be made to make the program more effective.

*Airborne warning and control system program (AWACS).*—The purpose of the evaluation was to review and evaluate the effectiveness of Customs involvement with the U.S. Air Force's airborne warning and control system and to recommend changes needed.

*Regional ADP survey.*—The purpose of this survey was to assess regional data processing systems, operations, equipment, personnel, and costs; identify problems and opportunities in this area; and make recommendations as appropriate.

*Accelerated cargo clearance and entry processing test.*—ACCEPT is an online computer system which identifies importations to be either examined or not examined physically. The evaluation of ACCEPT was to test the feasibility of the test system and recommend future enhancements or curtailments of it.

The findings and recommendations arrived at in these evaluations resulted in significant management improvements and the issuance of certain policy documents.

### New appropriation accounting system

The implementation in October 1980 of a new appropriation accounting system culminated a multiyear effort in Customs. The system has been designed to capture cost as well as funds control data. The automated general ledger will reflect data from other major accounting systems and subsystems.

The target date for submitting the system to the General Accounting Office for design approval is March 1981.

#### Management inspection program

A management inspection program was initiated to evaluate the overall management of Customs field activities. The inspections, while not designed to probe in depth into any specific program, provide a complete and accurate picture of the status of the management of field operations. In fiscal 1980, three of the nine regions were inspected and a followup inspection was conducted in a fourth.

## UNITED STATES SAVINGS BONDS DIVISION

On January 1, 1980, two new U.S. savings bonds—series EE and HH—went on sale at banks and through payroll savings plans.<sup>1</sup> Simultaneously, all series H bond sales, and all over-the-counter sales of series E bonds were discontinued. Some organizations, however, continued to offer E bonds on their payroll savings plans up to June 30, 1980.

Series EE and HH were the first new savings bonds offered to the public in 28 years. (H bonds went on sale in 1952, and series E bonds were first issued in 1941.)

On December 12, 1979, the future EE savings bonds underwent two major changes: Their time to maturity was shortened from 11¾ years to 11 years, and their interest rate was increased from 6.5 percent to 7 percent for bonds held to maturity.

The new EE and HH bonds were introduced during a period of extreme volatility in the economic and financial worlds. Interest rates on some other forms of savings and investments reached temporary peaks of more than 15 percent during the early months of 1980. Because of this, as well as the confusion arising from any major changes in a long-established program, bond sales of \$4.8 billion during 1980 were lower than the previous year. Redemptions were unusually high during the first half of the calendar year, but the figures improved in the last 6 months and were better than the comparable period in 1979.

#### Office of the National Director

The Office of the National Director includes the National and Deputy National Directors, the Office of Public Affairs, and the Office of Planning and Market Research.

The National Director, Deputy Director, and other senior officials conducted active speaking schedules on behalf of the savings bonds program as well as performed the personnel, budget, and supervisory functions essential during a year of major changes. All offices in the Office of the National Director were involved in the planning and implementation of the new EE and HH savings bonds program.

<sup>1</sup> See exhibits 4 and 5.

The Savings Bonds Division continues to operate with a staff of approximately 425 Treasury employees. This is augmented by an estimated 540,000 volunteers. A major responsibility of the Division is to motivate, inform, and assist these volunteers to organize bond drives in their industries, speak at bond rallies, write and produce advertisements for bonds, and perform other sales, informational, and promotional activities.

#### **U.S. industrial payroll savings campaign**

The U.S. Industrial Payroll Savings Committee, composed of 60 top business and industrial leaders, is a principal force behind the payroll savings program for private business.

E. Robert Kinney, chairman of the board and chief executive officer, General Mills, Inc., and chairman of the 1980 U.S. Industrial Payroll Savings Committee, began the yearly campaign with a meeting in Washington, D.C., on December 12, 1979. The luncheon meeting was highlighted by a speech from Secretary Miller and reports by outgoing Committee Chairman Harold J. Haynes and incoming Chairman Kinney.

Serving on the Committee with Mr. Kinney this year were the former chairmen and 46 top executives of the Nation's major corporations.

Members of the U.S. Industrial Payroll Savings Committee conduct meetings of top management people, urge chief executives in their areas and industries to conduct payroll savings drives, and set strong examples by conducting campaigns in their own companies.

Chairman Kinney contributed much of his own time and effort to the program. He traveled to 15 cities and addressed 17 meetings of business and community leaders between November 5, 1979, and March 8, 1980. He also provided some excellent sales tools for savings bonds volunteers, including a brochure for top executives entitled "Take Stock in America with Series EE, the Bond that Doubles," newsletters to volunteers to publicize the campaign, and a full-page ad in the Wall Street Journal featuring the 1980 Committee members. He also put a savings bonds message on 11 million packages of Wheaties cereal.

#### **The banking program and the ABA Savings Bonds Committee**

A major factor in the development of the savings bonds program has been the support of the Nation's banks and other financial institutions, which provide more than 39,000 over-the-counter sales outlets. They also provide bond-issuing services for the majority of companies on payroll savings plans. The consistent high quality delivery of issue, redemption, and information services by banks and other financial institutions is a necessary part of the savings bonds program.

The success of the banking program is largely due to the efforts of the American Bankers Association (ABA) Savings Bonds Committee. This committee, appointed by the president of the ABA, consists of a national chairman and a leading banker from each State and the District of Columbia who serve as State savings bonds coordinators. They support the program by bringing the savings bonds message to their peers through letters and meetings, as well as by providing leadership to the State savings bonds banking chairmen.

Financial institutions across the country are asked to: send a letter to their customers encouraging the purchase of savings bonds; help disseminate special information about some aspect of the savings bonds program by enclosing a savings bonds leaflet in a regular statement mailing; sponsor



savings bonds advertising in local media; conduct a savings bonds seminar; and prominently display savings bonds promotional materials in their lobby.

The 1980 ABA Savings Bonds Committee was chaired by John D. Chisholm, president of Marquette Bank and Trust Co. The Committee met in Washington, D.C., on November 5 and 6, 1979, to plan and launch the 1980 campaign.

Mr. Chisholm crisscrossed the country on behalf of the 1980 campaign, kicking off banking and retail merchandising industries' payroll savings campaigns and numerous "Take Stock in America" campaigns, and speaking at meetings of his fellow bankers.

To help eliminate the confusion about series E bonds occasioned by the introduction of the new bond, a special letter was sent to bankers by members of the ABA Savings Bonds Committee. The letter asked bankers to send their customers a letter advising them that their holdings were still earning interest and that no bonds would finally mature until May of 1981.

To assist banks in the transition effort, the Savings Bonds Division published and distributed "A Transition Guide for Financial Institutions," which outlined the steps necessary to switch customers over to series EE bonds. This was followed by national distribution of new reference and consumer information materials.

The American Institute of Banking, the ABA's largest educational arm, helped to train more than 100,000 bank personnel in handling series EE transactions, using the new savings bonds seminar program developed by the ABA in cooperation with Treasury.

#### Volunteer State Chairmen's Council

Volunteer support is basic to the savings bonds program's success. This support, at the State and county level, is directed through the Volunteer State Chairmen's Council made up of business leaders from each State and the District of Columbia. The Council has been serving the Nation, through the savings bonds program, since 1941.

Each chairman appoints and chairs a State committee whose members provide expertise in promoting bonds through advertising and publicity, banking, the Federal Government, organized labor, and "Take Stock in America" campaigns. Local leadership is provided by more than 3,000 county chairmen appointed by the respective State chairmen.

John V. James, chairman, president, and chief executive officer, Dresser Industries, and chairman of the Volunteer State Chairmen's Council, presided at the Council's annual meeting on November 5 and 6, 1979. At this meeting, the State chairmen focused on ways to make a successful transition to series EE bonds.

A 1980 Volunteer State Chairmen's Council brochure was published by Mr. James. Distributed to all State and county volunteers, it explained the rate increase and introduced an amplified plan for volunteer action, with special emphasis on promoting the payroll savings plan. This followed distribution of a savings bonds guide to volunteers.

To aid the State chairmen and their committees, and to provide consistency across the Nation, the chairman developed and published a Calendar of Events which provided a planning timetable for State chairmen. And to sustain program action at the local level, a campaign kit for volunteers was assembled and distributed to all county and local volunteers by the State chairmen.

### National organizations

In cooperation with the National Organizations Committee, chaired by Louis B. Clark, economics director of the American Legion, national associations helped to promote the new EE and HH savings bonds. Letters of endorsement were distributed to local chapters by a number of organizations. Savings bonds ads and articles were run in association publications, and local chapters conducted special savings bonds meetings and developed bond exhibits for banks, schools, libraries, and meeting places. Organizations with a total membership of 50 million supported the program. In addition, product information was distributed at conventions of organizations such as Kiwanis, The Loyal Order of Moose, the American Legion, and the Masons. Other associations ran articles in their magazines and made mailings to their membership.

The American Hospital Association sent new parents a special savings bonds message in the form of a child's measuring chart designed for retention and later use. Approximately 2,500,000 of these charts were distributed through hospitals in 1980.

### Labor support

The major goal of the labor program for 1980 was to expand and appoint members of the National Labor Committee. This was accomplished, and the Committee now has 11 members, including leaders of the AFL-CIO and of independent associations. All members were briefed personally on the change in product, given the latest factsheets on series EE bonds, and asked to send letters of endorsement to their membership. Members also sent statements pledging their support to the Savings Bonds Division and directly supported the program by editorials, advertising, and news stories in their labor publications.

Another goal was to provide recognition to 14 major unions at their national conventions. This forum was also used to present the latest changes in the bond program, obtain labor resolutions of endorsement, distribute promotional materials, and present supporters with labor and Treasury awards. Field staff members attended State AFL-CIO and independent association conventions throughout the year for the same purpose, and were able to canvass the membership and develop a cadre of volunteers to work in savings bonds campaigns. Numerous unions published articles and messages to inform their membership about series EE bonds.

The Office of National Labor Activities introduced a new dimension to the labor program called the L&M concept. The aim was to obtain labor's support for the 1980 Industrial Payroll Savings Committee Campaign chairmen. Cooperating national presidents of unions in such major industries as oil, rubber, steel, and automobiles were urged to send congratulatory letters to the chief executive officer of their industry's Savings Bonds Committee. Twelve union presidents responded favorably.

The nine working departments of the AFL-CIO are one of the major keys to labor cooperation in the savings bonds program. During fiscal 1980, presidents of six of the departments sent letters of endorsement to their affiliates.

A special labor kit was updated and sent to the 450 staff and field representatives of the Community Services Department for their use in promoting the savings bonds program at the community level.

Despite difficulties encountered in the transitional year of 1980, the goals for letters and leaflets sent were exceeded.

### Federal payroll savings campaign

One of the major goals of this program for 1980 was to begin and complete the transition from the sale of series E bonds to the sale of series EE bonds smoothly and with the least possible attrition. A method of payroll conversion which would preclude the necessity of recanvassing all purchasers of series E bonds was devised by the staff of the Federal Payroll Savings Office. By this method, the savings bonds allotment of an employee already enrolled would be automatically applied to the purchase of series EE bonds, unless that employee requested otherwise. This method was endorsed by the Comptroller General of the United States, thus erasing any uncertainties regarding the propriety of its use throughout the Federal Government.

Over 90 percent of departments and agencies of the Federal Government completed the transition by March 31, with the remainder completed by June 30. The decline in participation during the transition period is considered moderate in light of economic conditions and the higher attrition which would have resulted from a total recanvassing. With this method as a precedent, the path was opened for similar payroll savings conversions in private industry.

In December 1979, President Carter announced the appointment of Defense Secretary Harold Brown to the post of Interagency Savings Bonds Committee Chairman, and pledged his personal support for the program.

The campaign was kicked off on April 9, 1980, with a rally attended by more than 2,000 top Government officials, agency savings bonds coordinators, and canvassers. Featured speakers were Secretary Brown and baseball star Pete Rose of the Philadelphia Phillies, who served as the 1980 honorary chairman.

Despite the difficulties encountered in this transitional year, campaigns in the Federal sector yielded nearly 100,000 new enrollees in the payroll savings plan or increases in the allotment amounts of those already enrolled. The results of the campaign at the Department of the Treasury were slightly better than those for the Federal Government as a whole.

### Advertising support

Interesting and unusual ways in which Americans have used savings bonds continued to provide the theme for advertising. The Advertising Council estimated that more than 30,000 ads were published in newspapers, and some 290,000 lines appeared in national magazines.

The Nation's television stations broadcast over 100,000 savings bonds announcements during the year, and radio stations used almost 500,000 public service messages for savings bonds.

"The Bond Teller" assumed a major role in guiding and informing financial institutions about the series EE and HH bonds and the status of the series E bonds and savings notes. With volunteer involvement and participation substantially enlarged, the function of "Savings Bonds Salute" in providing recognition for this vital corps took on new importance.

In the annual savings bonds awards competition for company communicators—based on payroll savings promotion appearing in company publications in 1979—Marci Johnson of Dravo Corp. was named "Communicator of the Year." Presentation of this award and 25 others was made June 13, 1980, by the National Director at the Main Treasury Building.

An all-new copy kit for daily and weekly newspapers, and several feature articles for newspapers, were completed.



### Administration

Training functions, except for technical sales training of bond sales promotion representatives, were transferred from the Sales Branch to the Office of Personnel. This is expected to result in more timely and economical training of employees.

All procurement authority has now been consolidated in the Office of Property and Facilities Management. This change should assure that all procurements are made in accordance with regulatory requirements and in the most economical manner. It also frees staff in field offices to devote more of their time and energy to their primary function of promoting the sale and retention of U.S. savings bonds.

A performance appraisal plan for managers and supervisors eligible for merit pay was developed and partially implemented. Full implementation will be in effect by the end of the calendar year.

## UNITED STATES SECRET SERVICE

The major responsibilities of the U.S. Secret Service are defined in section 3056, title 18, United States Code. The investigative responsibilities are to detect and arrest persons committing any offense against the laws of the United States relating to coins, obligations, and securities of the United States and of foreign governments; and to detect and arrest persons violating certain laws relating to the Federal Deposit Insurance Corporation, Federal land banks, joint-stock land banks, and Federal land bank associations. The protective responsibilities include protection of the President of the United States and the members of his immediate family; the President-elect and the members of his immediate family; the Vice President or other officer next in the order of succession to the Office of the President, and the members of his immediate family; the Vice President-elect and the members of his immediate family; a former President and his wife during his lifetime; the widow of a former President until her death or remarriage; the minor children of a former President until they reach 16 years of age; a visiting head of a foreign state or foreign government; and, at the direction of the President, other distinguished foreign visitors to the United States and official representatives of the United States performing special missions abroad. In addition, Public Law 90-331, as amended, authorizes the Secret Service to protect major Presidential and Vice Presidential candidates; and upon request, the spouse of a major Presidential or Vice Presidential candidate, except that such protection shall not commence more than 120 days prior to the general Presidential election.

### Investigative operations

*Counterfeiting.*—The Secret Service seized \$55.3 million in counterfeit U.S. currency during fiscal 1980, \$5.5 million of which was passed on the public. The dollar amount represents a 20-percent increase over the record \$46.2 million seized in fiscal 1979. The number of notes passed increased by 1 percent, while the dollar amount increased by 23 percent. This is a result of an increase of 55 percent in the number of \$50 and \$100 denomination notes

passed over the totals for fiscal 1979. It is also consistent with the fact that more genuine \$50 and \$100 denomination notes are circulating now than ever before. Total number of printing operations suppressed increased by 24 percent to 78.

Of interest is the fact that 19 percent of the total amount passed on the American public was printed in Colombia, South America. The following case summaries illustrate several counterfeit investigations successfully concluded during fiscal 1980.

Oklahoma City. This case originated in May 1978 when a defendant provided the name of his source of counterfeit \$20 notes. Continued investigation established this source as the probable distributor of at least five different notes. During the next year, three persons were identified as having access to these bogus bills but attempts by undercover Secret Service agents to purchase these bills were unsuccessful. Between May and September 1979, negotiations to purchase notes from the source began to meet with some success. From September 22 through October 10, 24-hour surveillance was maintained on the source and two possible printers. On October 9, 1979, a delivery from one of the printers to the source was witnessed by agents. When a confidential informant confirmed the suspect was in possession of a large quantity of bogus bills, the suspect and the printer were arrested. Confiscated at that time was \$1.3 million in two new issues of counterfeit and the plates and negatives of all seven notes the suspects had printed over a 5-year period.

Bogota, Colombia. In March 1980, Secret Service special agents working in conjunction with police officials in Bogota, Colombia, successfully concluded investigations which resulted in the suppression of a counterfeiting plant and the seizure of \$12 million in counterfeit U.S. currency and 200 million pesos in counterfeit Colombian obligations. The five different counterfeit issues seized accounted for 7 percent of all Colombian origin notes passed on the American public in fiscal 1979.

San Francisco. In mid-January 1980, agents in the San Francisco field office concluded investigations resulting in the seizure of approximately \$4.5 million in counterfeit notes, the arrest of 11 defendants, and the suppression of 4 unrelated printing plants responsible for printing 15 different counterfeit issues.

Santa Barbara, Calif. On April 28, 1980, agents in the Los Angeles field office received a specimen of a previously unknown counterfeit \$100 Federal Reserve note from the Los Angeles County Sheriff's Department. Further investigation revealed the note had been produced in San Bernardino County, by individuals suspected of operating a phencyclidine (PCP) laboratory. Joint investigation between the Secret Service and local authorities developed sufficient probable cause to obtain search warrants for the premises. On May 1, 1980, the search warrants were executed at the suspected site and a complete printing operation, as well as \$2.3 million in new counterfeit \$100's and \$20's, was seized. An active PCP laboratory was suppressed by the San Bernardino County Sheriff's Department. Three suspects were arrested. All three defendants had extensive criminal histories and one had two previous arrests for counterfeiting.

*Check forgery.*—During fiscal 1980, the Service received 65,808 checks for investigation and made 3,647 check forgery arrests. Treasury paid approximately 680 million checks during fiscal 1980. The Service received 97 checks per million paid, or 1 check for investigation for approximately 7,010 checks paid. Some examples of check forgery investigative cases follow:

Columbia, S.C. Between October 1974 and September 1979, an employee of the Veterans Administration in Columbia, who controlled records dealing with veterans pensions, created 14 nonexistent pensions; caused Treasury checks and direct deposit monies to be issued; and diverted the money to her use. The employee used four separate post office boxes and maintained accounts at several different area banks. Over 500 checks were issued and forged, defrauding the Government in excess of \$234,000. The fraud might have continued undetected had it not been for an alert bank teller who suspected a check-kiting activity. In January 1980, the defendant began serving a 5-year prison sentence.

Salt Lake City, Utah. During early 1980, the comptroller for a company in Salt Lake City issued over 100 fraudulent W-2 forms; then filed fictitious income tax returns using the names and social security numbers of job applicants at his company. As a result tax refund checks, averaging approximately \$3,800 each, were issued. A suspicious bank teller and a subsequent citywide bank alert exposed the fact that numerous fictitious bank accounts had been opened in the Salt Lake City area with the monies eventually being traced back to the comptroller. On April 28, 1980, the comptroller was arrested and charged with forgery. He was subsequently sentenced to serve 3 years in prison.

*Bond forgery.*—During fiscal 1980, the number of bonds received for forgery investigation dropped for the fourth consecutive year—with 8,242 bonds received for investigation, as compared with 9,624 last fiscal year. Ninety-one persons were arrested for bond forgery.

The Secret Service recovered, prior to forgery and redemption, 6,037 stolen bonds with a face value of \$996,200, compared with fiscal 1979 when 9,455 stolen bonds were recovered with a face value of \$787,070. The summary of a bond forgery investigation follows.

Miami. Between April 13 and 20, 1980, the residence of an Oaklyn, N.J., registered owner was burglarized. During the burglary, the following items were taken: \$12,000 in series E savings bonds, savings account passbooks, certificates of deposit, personal checks, the registered owner's U.S. passport, social security card, and several credit cards. An investigation by the Oaklyn Police determined that several of the stolen personal checks were negotiated by an individual using a Florida driver's license.

On May 9, 1980, a woman purporting to be the registered owner opened a savings account at the Commercial Bank of Kendall, Miami, Fla., using one of the stolen \$1,000 U.S. savings bonds and presenting the stolen U.S. passport for identification. Three days later, the same individual redeemed three additional bonds and, at that time, presented a savings bank passbook for closing.

On May 23, 1980, a woman identifying herself as the registered owner telephoned the Commercial Bank of Kendall requesting the status of the bank draft closing the savings account. She was advised that it would be arriving at the bank on May 27, 1980, with the 1:00 p.m. mail.

On May 27, 1980, a surveillance was conducted by agents of the Secret Service and local authorities; however, the suspect did not appear at the bank during normal working hours. Later that day a beige van with New Jersey license plates was located at a nearby motel. Inquiry at the motel revealed that the suspect was registered. As agents were setting up a surveillance at the motel the van departed. It was stopped and the occupants arrested. A search of the van produced two handguns and the stolen property of the registered owner along with a large supply of drugs. The passengers were identified as Federal fugitives. It was determined that the van was stolen from New



Jersey. The defendants are currently serving a 2-year sentence on a previous forgery indictment, leaving judicial action pending in this case.

Throughout the fiscal year, while experiencing peak levels of protective activities in connection with the 1980 Presidential campaign requirements, the Secret Service has continued to fulfill its priority investigations.

#### Identification Branch

The Identification Branch of the Special Investigations and Security Division serves all field offices by conducting technical examinations of handwriting, handprinting, typewriting, fingerprints, palmprints, striations on counterfeit currency, altered documents, and other types of physical evidence.

During fiscal 1980, members of the Identification Branch conducted examinations in 5,556 cases involving 377,068 exhibits. This resulted in 1,701 identifications of persons and a total of 219 court appearances to furnish expert testimony.

#### Treasury Security Force

The Treasury Security Force, a uniformed branch of the U.S. Secret Service, protects the Main Treasury and Treasury Annex Buildings, and participates in providing security for the White House. It also conducts investigations involving petty larceny cases, theft, and other improper actions which take place on Treasury premises.

During fiscal 1980, the Force interviewed 181 persons for attempted unauthorized entry into the Treasury Buildings, and conducted 118 other investigations involving misdemeanor violations.

#### Protective operations

During fiscal 1980, the Secret Service provided protection for the President and Mrs. Carter, and members of their family; Vice President and Mrs. Mondale, and members of their family; former President and Mrs. Ford; former President and Mrs. Nixon; and former First Ladies Mrs. Harry S. Truman and Mrs. Lyndon B. Johnson.

During this time, President Carter made domestic trips to 130 cities and foreign trips to Rome, Venice, Belgrade, Madrid, and Lisbon in June 1980, and to Tokyo the following month. The First Lady traveled to 276 cities domestically and made foreign trips to Japan, Thailand, and Canada in November 1979; Rome, Venice, Belgrade, Madrid, and Lisbon with the President in June 1980; and Peru in July 1980.

The Vice President and Mrs. Mondale made numerous domestic visits this year as well as foreign trips to Senegal, Niger, Nigeria, and Cape Verde in July 1980. Vice President Mondale also attended President Tito's funeral in Belgrade, Yugoslavia, in May 1980.

Former President Ford visited Tokyo, Japan, in late August 1980.

Former President Nixon visited Paris and the Ivory Coast during March 1980. From mid-April through early May he visited Germany, Spain, France, and England. During the summer he visited France, Switzerland, Germany, and Egypt.

Former First Lady Mrs. Lyndon B. Johnson visited Mexico during late January and early February 1980; Egypt and England during late March and early April 1980; and spent 6 weeks in England and Spain in August and September 1980.

Foreign dignitary protection remained a major effort during fiscal 1980. Preliminary preparations were made for the protection of 144 foreign dignitaries; however, subsequent declinations and cancellations reduced this number to 102. These included 100 visits by heads of a foreign state or government and 2 other distinguished visitors to the United States. Large-scale protective endeavors included the visits of Pope John Paul II, Premier Fidel Castro of Cuba, and the opening session of U.N. General Assembly No. 34. Further, protection was provided for 18 foreign heads of state or government for the 35th session of the U.N. General Assembly in September.

Protection was provided for major Presidential and Vice Presidential candidates and nominees during the 1980 Presidential campaign. The Candidate/Nominee Protective Division became operational on September 10, 1979, and later that month candidate protection commenced for Senator Kennedy. Later in 1979, protection began for Governor Reagan, and in 1980 for Senator Baker, Congressman Crane, Congressman Anderson, and former Ambassador Bush. During this period, the candidates made 2,326 trips which included 6,321 sites.

During fiscal 1980, the U.S. Secret Service Uniformed Division continued to provide protection for the White House, Presidential offices, the official residence of the Vice President, the Blair House when occupied by visiting heads of state, and foreign diplomatic missions of 136 countries at 407 locations within the Washington metropolitan area. In addition, the Uniformed Division participated in the protection of Fidel Castro during his visit to New York City and provided security to the Iranian mission to the United Nations. Uniformed Division support units, Counter-Sniper and Canine, assisted the Service in providing protection to major Presidential candidates during the campaign period.

#### Protective research

During fiscal 1980, the Secret Service contracted a study into the feasibility of developing a personality assessment/behavior prediction methodology to evaluate individuals suspected of threatening the life of the President and others.

In conjunction with the 1980 campaign year, the national press credential system was implemented. The system provided uniform credentialing of members of the press and eliminated the requirement of individual issuance for every campaign event. The system resulted in considerable time savings for the Service and members of the media.

Several types of intrusion detection sensors for outdoor perimeter security were purchased. Also, test and evaluation programs of armoring materials and electronic security equipment continued.

The Communications and Technical Development and Planning Divisions received delivery of production units of voice privacy equipment to modify a portion of the Service's present VHF radios.

Radio system installations and improvements were accomplished in several field offices. A secure voice telephone terminal was installed in the New York office as a prototype for future installations. The Communications Division also installed State and local criminal information system terminals in five field offices.

The Protective Research Divisions provide technical surveillance counter-measures in the White House complex.

The Data Systems and Communications Divisions expended a major effort in the installation and operation of computer and communications equipment in support of the Secret Service Campaign 1980 commitment.

Technical Security Division personnel were trained in technical aspects of rail and marine operations, to provide increased security for protectees using those modes of transportation.

New baggage inspection procedures were installed at the VIP departure area at Andrews Air Force Base.

Personal contact was maintained by Liaison Division personnel with Federal law enforcement agencies, the intelligence community, and other Federal agencies. This liaison duty assures proper coordination, communications, and exchange of information in matters relating to Secret Service protective and criminal investigative responsibilities.

The Freedom of Information Branch processed 670 Freedom of Information Act requests and 96 Privacy Act requests during fiscal 1980.

#### Administration

A study of Treasury payroll/personnel information system (TPPIS) operations in the Secret Service was conducted to analyze utilization and internal manageability. Based on collected data, the feasibility of structuring a distinct TPPIS organization in the Service is being studied.

The problem of a high motor vehicle accident rate in the Uniformed Division motor scooter patrol was studied. Experts from the traffic safety, motorcycle manufacturing, and training communities, and State and local police departments were canvassed. Underlying trends and patterns were identified. The final report should affect the training, equipment, and utilization of motor scooters to reduce accidents.

A network of nine airline teleticketing machines has been installed. The implementation of teleticketing was based on demonstrated savings realized through a reduction in issuing GTR's (Government transportation requests) and related processing costs.

A directive prescribing policies and procedures and encompassing guidelines for the planning, procurement, and use of ADP resources, and requiring periodic internal reviews of ADP applications and installations, was developed and issued to Service managers.

The Candidate/Nominee protective division manual, which provides policy and procedural guidance during Presidential election campaigns, was revised.

In the area of energy conservation 25 percent of the replacement vehicles ordered in fiscal 1980 were equipped with 302-cubic-inch engines expected to result in fuel consumption savings. Performance of these vehicles will be monitored to determine if future purchases of vehicles with smaller engines are warranted.

A contract was awarded to a commercial vendor and service was implemented during fiscal 1980 for microfiche replacement of paper output for the automated accounting system. Substantial savings are being realized because of the elimination of microfilming and the reduction of computer run time, and space costs.

A Secret Service performance appraisal system was developed as required by the Civil Service Reform Act of 1978. The new appraisal standards and elements will be in place by October 1980 for merit pay employees, GS-13 through GS-15. Performance appraisal standards and elements for nonmerit pay employees are being readied to go into effect in October 1981.

An increase in employee use of the employee assistance program has resulted in the hiring of an additional counselor to provide confidential nationwide counseling and referral services to employees with problems affecting job performance.



## Training

There were 97,617 staff-hours of training conducted by the Office of Training during fiscal 1980. In addition, 29,000 staff-hours of interagency and 9,054 staff-hours of nongovernment training were completed for a total of 135,671 staff-hours. Because of commitments for candidate/nominee protection there was some increase in training this fiscal year.

Training courses conducted in fiscal 1980 focused upon preparing both Service and non-Service personnel to meet the protective responsibilities of the 1980 Presidential campaign. Some of the highlights of the courses conducted in protection follow:

Four courses were developed and implemented to meet 1980 Presidential campaign needs: Candidate/nominee briefings, candidate/nominee operations, detail supervisors' briefings, and SAIC conferences. There were 588 Service personnel attending these courses that ranged from 2 to 4 days.

Also in preparation for the 1980 Presidential campaign twenty-one 3-day regional briefings were conducted to train 604 special agents from other Treasury law enforcement bureaus who had been selected for temporary assignments. In addition, 51 regional briefings were conducted for 1,500 other Treasury agents designated to support the Service in local post standing assignments.

Counterassault team tactics training was conducted, enabling agents assigned to protective details to respond quickly and effectively to a terrorist attack.

An extensive 21-week program was conducted for K-9 explosives detection teams. The training enabled teams to detect vapors given off by all known types of explosives.

To neutralize the potential threat of a sniping assault upon a protectee, countersniper training was conducted for uniformed personnel.

To insure safe and proficient use of firearms, approximately 30,000 individual courses of fire were conducted for personnel of the Secret Service and 1,700 employees of 23 other Federal law enforcement agencies required to carry firearms. Additionally, 20 employees of other Federal, State, and local agencies were trained to be firearms instructors.

While committed to the candidate/nominee program protective efforts, essential entry level, and specialized training needs were met also. These included: Special agent, uniformed specialized recruit, administrative personnel, computer fraud investigation, protective details, protective operations, questioned documents, stress management, technical security advance procedures, Blair House security, Cuban mission detail, Ford detail, and inservice training for uniformed officers and sergeants.

Over 200 officials from other Federal, State, and local agencies participated in 4 dignitary protection seminars and 2 protective operations briefings. To improve skills and enhance coordination in the area of protection, 50 protective seminars were conducted for 1,700 personnel from other State and local law enforcement agencies and campaign staffs.

In addition to these programs, the Office of Training conducted specialized security surveys for various public agencies, directed several interorganizational research projects, and offered individual and small group briefings when the participants' inclusion in a programmed course was impractical.

## Inspection

The Office of Inspection conducted 34 office inspections in fiscal 1980. In addition, other indepth studies and reviews were completed.

Inspectors were diverted from their regular duties to serve as supervisors on several temporary protective assignments, or as Acting Special Agents in Charge in field offices experiencing prolonged vacancies.

Two inspectors served as coordinators in the planning and operation of the Candidate/Nominee Protective Division. Another inspector was assigned to coordinate Secret Service protective operations for the Democratic National Convention. Since October 1979, inspectors have been involved as coordinators or detail leaders for protective details with Senators Kennedy and Baker, Congressmen Anderson and Crane, Governor Reagan, and Ambassador Bush.

Internal auditors conducted several audits during fiscal 1980. These reviews resulted in numerous recommendations for improved accountability and control over Secret Service property, cost avoidances, and actual cost recoveries.

#### Legal counsel

During fiscal 1980, the Secret Service initiated several legislative proposals. The first would amend title 18 of the United States Code by creating a new section relating to threats against Presidential candidates and certain other Secret Service protectees presently not covered by section 871 of title 18, United States Code, the Presidential threat statute. This proposal was initiated in response to recommendations of the House Select Committee on Assassinations and a subcommittee of the Senate Committee on Appropriations after a review of Secret Service protective activities. This proposal was received by the Senate Judiciary Committee and was subsequently referred to the House Judiciary Committee on April 24, 1980.

The second proposal would amend section 1752 of title 18 of the United States Code, and authorize the Secretary to establish "secure areas" around the residences, offices, and temporary physical locations of persons authorized to receive Secret Service protection. "Secure areas" presently are authorized only for the President, but are essential to security.

The third proposal would amend chapter 25 of title 18, United States Code, and add a new section 510 making it a Federal crime to forge, alter endorsements on, or fraudulently negotiate U.S. obligations or securities. This new section would enable the Secret Service to more adequately prosecute criminal forgery cases. This proposal was referred to the Senate Judiciary Committee.

The fourth legislative proposal would amend the D.C. Police and Fireman's Salary Act to provide the same cost-of-living adjustments for employees of the Secret Service Uniformed Division as are given to Federal employees under the General Schedule. This proposal is modeled after Public Law 94-533 which applies to the U.S. Park Police.

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## EXHIBITS

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## Public Debt Operations, Regulations, and Legislation

### Exhibit 1.—Treasury notes

A Treasury circular covering an auction for cash with an interest rate determined through competitive bidding is reproduced in this exhibit. Circulars pertaining to the other note offerings during fiscal 1980 are similar in form and therefore are not reproduced in this report. However, essential details for each offering are summarized in the table in this exhibit, and allotment data for the new notes will be shown in table 37 in the Statistical Appendix. During the year there were no offerings in which holders of maturing securities were given preemptive rights to exchange their holdings for new notes.

#### DEPARTMENT CIRCULAR NO. 28-79. PUBLIC DEBT

DEPARTMENT OF THE TREASURY,  
*Washington, November 14, 1979.*

##### 1. INVITATION FOR TENDERS

1.1. The Secretary of the Treasury, under the authority of the Second Liberty Bond Act, as amended, invites tenders for approximately \$4,300,000,000 of United States securities, designated Treasury Notes of November 30, 1981, Series Z-1981 (CUSIP No. 912827 KD 3). The securities will be sold at auction with bidding on the basis of yield. Payment will be required at the price equivalent of the bid yield of each accepted tender. The interest rate on the securities and the price equivalent of each accepted bid will be determined in the manner described below. Additional amounts of these securities may be issued to Government accounts and Federal Reserve Banks for their own account in exchange for maturing Treasury securities. Additional amounts of the new securities may also be issued at the average price to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing securities held by them.

##### 2. DESCRIPTION OF SECURITIES

2.1. The securities will be dated November 30, 1979, and will bear interest from that date, payable on a semiannual basis on May 31, 1980, and each subsequent 6 months on November 30 and May 31, until the principal becomes payable. They will mature November 30, 1981, and will not be subject to call for redemption prior to maturity.

2.2. The income derived from the securities is subject to all taxes imposed under the Internal Revenue Code of 1954. The securities are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, any possession of the United States, or any local taxing authority.

2.3. The securities will be acceptable to secure deposits of public monies. They will not be acceptable in payment of taxes.

2.4. Bearer securities with interest coupons attached, and securities registered as to principal and interest, will be issued in denominations of \$5,000, \$10,000, \$100,000, and \$1,000,000. Book-entry securities will be available to eligible bidders in multiples of those amounts. Interchanges of securities of different denominations and of coupon, registered and book-entry securities, and the transfer of registered securities will be permitted.

2.5. The Department of the Treasury's general regulations governing United States securities apply to the securities offered in this circular. These general regulations include those currently in effect, as well as those that may be issued at a later date.

### 3. SALE PROCEDURES

3.1. Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Wednesday, November 21, 1979. Noncompetitive tenders as defined below will be considered timely if postmarked no later than Tuesday, November 20, 1979.

3.2. Each tender must state the face amount of securities bid for. The minimum bid is \$5,000 and larger bids must be in multiples of that amount. Competitive tenders must also show the yield desired, expressed in terms of an annual yield with two decimals, e.g., 7.11%. Common fractions may not be used. Noncompetitive tenders must show the term "noncompetitive" on the tender form in lieu of a specified yield. No bidder may submit more than one noncompetitive tender and the amount may not exceed \$1,000,000.

3.3. All bidders must certify that they have not made and will not make any agreements for the sale or purchase of any securities of this issue prior to the deadline established in Section 3.1. for receipt of tenders. Those authorized to submit tenders for the account of customers will be required to certify that such tenders are submitted under the same conditions, agreements, and certifications as tenders submitted directly by bidders for their own account.

3.4. Commercial banks, which for this purpose are defined as banks accepting demand deposits, and primary dealers, which for this purpose are defined as dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, may submit tenders for account of customers if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account.

3.5. Tenders will be received without deposit for their own account from commercial banks and other banking institutions; primary dealers, as defined above; Federally-insured savings and loan associations; States, and their political subdivisions or instrumentalities; public pension and retirement and other public funds; international organizations in which the United States holds membership; foreign central banks and foreign states; Federal Reserve Banks; and Government accounts. Tenders from others must be accompanied by a deposit of 5% of the face amount of securities applied for (in the form of cash, maturing Treasury securities or readily collectible checks), or by a guarantee of such deposit by a commercial bank or a primary dealer.

3.6. Immediately after the closing hour, tenders will be opened, followed by a public announcement of the amount and yield range of accepted bids. Subject to the reservations expressed in Section 4, noncompetitive tenders will be accepted in full, and then competitive tenders will be accepted, starting with those at the lowest yields, through successively higher yields to the extent required to attain the amount offered. Tenders at the highest accepted yield will be prorated if necessary. After the determination is made as to which tenders are accepted, a coupon rate will be established, on the basis of a  $\frac{1}{8}$  of one percent increment, which results in an equivalent average accepted price close to 100.000 and a lowest accepted price above the original issue discount limit of 99.500. That rate of interest will be paid on all of the securities. Based on such interest rate, the price on each competitive tender allotted will be determined and each successful competitive bidder will be required to pay the price equivalent to the yield bid. Those submitting noncompetitive tenders will pay the price equivalent to the weighted average yield of accepted competitive tenders. Price calculations will be carried to three decimal places on the basis of price per hundred, e.g., 99.923, and the determinations of the Secretary of the Treasury shall be final. If the amount of noncompetitive tenders received would absorb all or most of the offering, competitive tenders will be accepted in an amount sufficient to provide a fair determination of the yield. Tenders received from Government accounts and Federal Reserve Banks will be accepted at the price equivalent to the weighted average yield of accepted competitive tenders.

3.7. Competitive bidders will be advised of the acceptance or rejection of their tenders. Those submitting noncompetitive tenders will only be notified if the tender is not accepted in full, or when the price is over par.



#### 4. RESERVATIONS

4.1. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders in whole or in part, to allot more or less than the amount of securities specified in Section 1, and to make different percentage allotments to various classes of applicants when the Secretary considers it in the public interest. The Secretary's action under this Section is final.

#### 5. PAYMENT AND DELIVERY

5.1. Settlement for allotted securities must be made or completed on or before Friday, November 30, 1979, at the Federal Reserve Bank or Branch or at the Bureau of the Public Debt, wherever the tender was submitted. Payment must be in cash; in other funds immediately available to the Treasury; in Treasury bills, notes or bonds (with all coupons detached) maturing on or before the settlement date but which are not overdue as defined in the general regulations governing United States securities; or by check drawn to the order of the institution to which the tender was submitted, which must be received at such institution no later than:

- (a) Tuesday, November 27, 1979, if the check is drawn on a bank in the Federal Reserve District of the institution to which the check is submitted (the Fifth Federal Reserve District in case of the Bureau of the Public Debt), or
- (b) Monday, November 26, 1979, if the check is drawn on a bank in another Federal Reserve District.

Checks received after the dates set forth in the preceding sentence will not be accepted unless they are payable at the applicable Federal Reserve Bank. Payment will not be considered complete where registered securities are requested if the appropriate identifying number as required on tax returns and other documents submitted to the Internal Revenue Service (an individual's social security number or an employer identification number) is not furnished. When payment is made in securities, a cash adjustment will be made to or required of the bidder for any difference between the face amount of securities presented and the amount payable on the securities allotted.

5.2. In every case where full payment is not completed on time, the deposit submitted with the tender, up to 5 percent of the face amount of securities allotted, shall, at the discretion of the Secretary of the Treasury, be forfeited to the United States.

5.3. Registered securities tendered as deposits and in payment for allotted securities are not required to be assigned if the new securities are to be registered in the same names and forms as appear in the registrations or assignments of the securities surrendered. When the new securities are to be registered in names and forms different from those in the inscriptions or assignments of the securities presented, the assignment should be to "The Secretary of the Treasury for (securities offered by this circular) in the name of (name and taxpayer identifying number)." If new securities in coupon form are desired, the assignment should be to "The Secretary of the Treasury for coupon (securities offered by this circular) to be delivered to (name and address)." Specific instructions for the issuance and delivery of the new securities, signed by the owner or authorized representative, must accompany the securities presented. Securities tendered in payment should be surrendered to the Federal Reserve Bank or Branch or to the Bureau of the Public Debt, Washington, D. C. 20226. The securities must be delivered at the expense and risk of the holder.

5.4. If bearer securities are not ready for delivery on the settlement date, purchasers may elect to receive interim certificates. These certificates shall be issued in bearer form and shall be exchangeable for definitive securities of this issue, when such securities are available, at any Federal Reserve Bank or Branch or at the Bureau of the Public Debt, Washington, D. C. 20226. The interim certificates must be returned at the risk and expense of the holder.

5.5. Delivery of securities in registered form will be made after the requested form of registration has been validated, the registered interest account has been established, and the securities have been inscribed.

## 6. GENERAL PROVISIONS

6.1. As fiscal agents of the United States, Federal Reserve Banks are authorized and requested to receive tenders, to make allotments as directed by the Secretary of the Treasury, to issue such notices as may be necessary, to receive payment for and make delivery of securities on full-paid allotments, and to issue interim certificates pending delivery of the definitive securities.

6.2. The Secretary of the Treasury may at any time issue supplemental or amendatory rules and regulations governing the offering. Public announcement of such changes will be promptly provided.

GERALD MURPHY,  
*Acting Fiscal Assistant Secretary.*

SUPPLEMENT TO DEPARTMENT CIRCULAR NO. 28-79. PUBLIC  
DEBT

DEPARTMENT OF THE TREASURY,  
*Washington, November 23, 1979.*

The Secretary announced on November 21, 1979, that the interest rate on the notes designated Series Z-1981, described in Department Circular—Public Debt Series—No. 28-79, dated November 14, 1979, will be  $12\frac{1}{8}$  percent. Interest on the notes will be payable at the rate of  $12\frac{1}{8}$  percent per annum.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

Summary of information pertaining to Treasury notes issued during fiscal year 1980

Date of preliminary announcement	Department circular		Concurrent offering circular No.	Treasury notes issued (all auctioned for cash)	Type of auction <sup>1</sup>	Accepted tenders		Minimum denomination	Issue date	Maturity date	Date tenders received	Payment date <sup>2</sup>
	No.	Date				Average price	High price					
1979												
Sept. 18	21-79	Sept. 19	22-79	10½ percent of X-1981	..... Yield	99.851	99.869	5,000	1979 Oct. 9	Sept. 30, 1981	1979 Oct. 3	1979 Oct. 9
Sept. 18	22-79	Sept. 19	21-79	9½ percent of F-1983	..... Yield	99.871	99.871	1,000	1979 Oct. 10	Sept. 30, 1983	1979 Oct. 4	1979 Oct. 10
Oct. 16	24-79	Oct. 17	.....	12½ percent of Y-1981	..... Yield	99.940	100.129	5,000	1979 Oct. 31	Oct. 31, 1981	1979 Oct. 23	1979 Oct. 31
Oct. 24	25-79	Oct. 25	26-79	11½ percent of G-1983	..... Yield	99.958	100.014	5,000	1979 Nov. 15	May 15, 1983	1979 Oct. 30	1979 Nov. 15
Oct. 24	26-79	Oct. 25	25-79	10½ percent of B-1989	..... Yield	100.000	100.303	5,000	1979 Nov. 15	Nov. 15, 1989	1979 Oct. 31	1979 Nov. 15
Nov. 13	28-79	Nov. 14	.....	12½ percent of Z-1981	..... Yield	99.801	99.905	5,000	1979 Nov. 30	Nov. 30, 1981	1979 Nov. 21	1979 Nov. 30
Nov. 20	29-79	Nov. 21	.....	10½ percent of C-1985	..... Yield	99.898	100.389	5,000	1979 Dec. 4	May 15, 1985	1979 Nov. 27	1979 Dec. 4
Dec. 12	30-79	Dec. 13	31-79	11½ percent of AB-1981	..... Yield	99.904	99.922	5,000	1979 Dec. 31	Dec. 31, 1981	1979 Dec. 19	1979 Dec. 31
Dec. 12	31-79	Dec. 13	30-79	10½ percent of H-1983	..... Yield	99.936	100.353	1,000	1979 Dec. 31	Dec. 31, 1983	1979 Dec. 20	1979 Dec. 31
1980												
Jan. 16	4-80	Jan. 17	.....	11½ percent of N-1982	..... Yield	99.965	100.000	5,000	1980 Jan. 31	Jan. 31, 1982	1980 Jan. 23	1980 Jan. 31
Jan. 30	5-80	Jan. 31	6-80	11½ percent of J-1983	..... Yield	99.707	100.014	5,000	1980 Feb. 15	Aug. 15, 1983	1980 Feb. 5	1980 Feb. 15
Jan. 30	6-80	Jan. 31	5-80	12 percent of C-1987	..... Yield	99.742	99.932	1,000	1980 Feb. 15	May 15, 1987	1980 Feb. 6	1980 Feb. 15
Feb. 13	8-80	Feb. 14	.....	13½ percent of P-1982	..... Yield	99.822	99.941	5,000	1980 Feb. 29	Feb. 28, 1982	1980 Feb. 20	1980 Feb. 29
Feb. 19	9-80	Feb. 20	.....	14½ percent of D-1985	..... Yield	99.758	100.443	1,000	1980 Mar. 3	May 15, 1985	1980 Feb. 26	1980 Mar. 3
Mar. 12	10-80	Mar. 13	11-80	15 percent of Q-1982	..... Yield	99.983	100.101	5,000	1980 Mar. 31	Mar. 31, 1982	1980 Mar. 20	1980 Mar. 31
Mar. 12	11-80	Mar. 13	10-80	14½ percent of D-1984	..... Yield	99.881	100.149	1,000	1980 Mar. 31	Mar. 31, 1984	1980 Mar. 25	1980 Mar. 31
Apr. 16	13-80	Apr. 17	.....	11½ percent of R-1982	..... Yield	99.887	99.939	5,000	1980 Apr. 30	Apr. 30, 1982	1980 Apr. 22	1980 Apr. 30
Apr. 30	14-80	May 1	15-80	16-80 9½ percent of K-1983	..... Yield	99.706	99.816	5,000	1980 May 15	Aug. 15, 1983	1980 May 6	1980 May 15
Apr. 30	15-80	May 1	14-80	16-80 10½ percent of B-1989	..... Price	105.27	106.10	1,000	1980 May 15	Nov. 15, 1989	1980 May 7	1980 May 15
May 14	17-80	May 15	.....	9½ percent of S-1982	..... Yield	100.009	100.151	5,000	1980 June 4	May 31, 1982	1980 June 2	1980 June 4
May 21	18-80	May 22	.....	9 percent of E-1985	..... Yield	99.775	100.177	5,000	1980 June 5	Aug. 15, 1985	1980 June 3	1980 June 5
June 13	19-80	June 16	20-80	8½ percent of T-1982	..... Yield	99.991	100.135	5,000	1980 June 30	June 30, 1982	1980 June 19	1980 June 30
June 13	20-80	June 16	19-80	8½ percent of E-1984	..... Yield	99.621	99.785	1,000	1980 June 30	June 30, 1984	1980 June 24	1980 June 30
July 15	22-80	July 16	.....	8½ percent of U-1982	..... Yield	99.830	99.919	5,000	1980 July 31	July 31, 1982	1980 July 23	1980 July 31
July 30	23-80	July 31	24-80	25-80 9½ percent of L-1983	..... Yield	99.873	99.955	5,000	1980 Aug. 15	Nov. 15, 1983	1980 Aug. 5	1980 Aug. 15
July 30	24-80	July 31	23-80	25-80 10½ percent of A-1990	..... Yield	99.639	100.121	1,000	1980 Aug. 15	Aug. 15, 1990	1980 Aug. 6	1980 Aug. 15



## Summary of information pertaining to Treasury notes issued during fiscal year 1980—Continued

Date of preliminary announcement	Department circular		Concurrent offering circular No.	Treasury notes issued (all auctioned for cash)	Type of auction <sup>1</sup>	Accepted tenders			Minimum denomination	Issue date	Maturity date	Date tenders received	Payment date <sup>2</sup>
	No.	Date				Average price	High price	Low price					
1980													
Aug. 12	26-80	Aug. 13			Yield	99.799	99.904	99.765	5,000	Sept. 2	Aug. 31, 1982	Aug. 20	Sept. 2
Aug. 19	27-80	Aug. 20		11½ percent of V-1982	Yield	99.835 <sup>3</sup>	100.103	99.759	1,000	Sept. 3	Nov. 15, 1985	Aug. 27	Sept. 3
Sept. 12	28-80	Sept. 15	29-80	11¾ percent of F-1985	Yield	99.905 <sup>3</sup>	100.043	99.853	5,000	Sept. 30	Sept. 30, 1982	Sept. 18	Sept. 30
Sept. 12	29-80	Sept. 15	28-80	11¾ percent of W-1982	Yield	99.985	100.233	99.923	1,000	Sept. 30	Sept. 30, 1984	Sept. 23	Sept. 30
				12½ percent of F-1984	Yield								
1980													
Aug. 12	26-80	Aug. 13			Yield	99.799	99.904	99.765	5,000	Sept. 2	Aug. 31, 1982	Aug. 20	Sept. 2
Aug. 19	27-80	Aug. 20		11½ percent of V-1982	Yield	99.835 <sup>3</sup>	100.103	99.759	1,000	Sept. 3	Nov. 15, 1985	Aug. 27	Sept. 3
Sept. 12	28-80	Sept. 15	29-80	11¾ percent of F-1985	Yield	99.905 <sup>3</sup>	100.043	99.853	5,000	Sept. 30	Sept. 30, 1982	Sept. 18	Sept. 30
Sept. 12	29-80	Sept. 15	28-80	11¾ percent of W-1982	Yield	99.985	100.233	99.923	1,000	Sept. 30	Sept. 30, 1984	Sept. 23	Sept. 30
				12½ percent of F-1984	Yield								

<sup>1</sup> All auctions but one for issues of notes were by the "yield" method in which bidders were required to bid on the basis of an annual yield; one issue of notes was by the "price" method, in which case the interest rate was announced prior to the auction and bidders were requested to bid a price. After tenders were allotted in the "yield" method auction, an interest rate for the notes was established at the nearest one-eighth of 1 percent increment that translated into an average accepted price close to 100.000.

<sup>2</sup> Payment could not be made through Treasury tax and loan accounts.

<sup>3</sup> Relatively small amounts of bids were accepted at a price or prices above the high shown. However, the higher price or prices are not shown in order to avoid an appreciable discontinuity in the range of prices, which would make it misrepresentative.

**Exhibit 2.—Treasury bonds**

A Treasury circular covering an auction of Treasury bonds for cash is reproduced in this exhibit. Circulars pertaining to other bond offerings during fiscal 1980 are similar in form and therefore are not reproduced in this report. However, essential details for each offering are summarized in the table in this exhibit, and allotment data for the bonds will be shown in table 38 in the Statistical Appendix. During the year there were no offerings in which holders of maturing securities were given preemptive rights to exchange their holdings for new bonds.

**DEPARTMENT CIRCULAR NO. 16-80. PUBLIC DEBT**

DEPARTMENT OF THE TREASURY,  
*Washington, May 1, 1980.*

**1. INVITATION TO TENDERS**

1.1. The Secretary of the Treasury, under the authority of the Second Liberty Bond Act, as amended, invites tenders for approximately \$2,000,000,000 of United States securities, designated Treasury Bonds of 2005-2010 (CUSIP No. 912810 CP 1). The securities will be sold at auction with bidding on the basis of yield. Payment will be required at the price equivalent of the bid yield of each accepted tender. The interest rate on the securities and the price equivalent of each accepted bid will be determined in the manner described below. Additional amounts of these securities may be issued to Government accounts and Federal Reserve Banks for their own account in exchange for maturing Treasury securities. Additional amounts of the new securities may also be issued at the average price to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing securities held by them.

**2. DESCRIPTION OF SECURITIES**

2.1. The securities will be dated May 15, 1980, and will bear interest from that date, payable on a semiannual basis on November 15, 1980, and each subsequent 6 months on May 15 and November 15, until the principal becomes payable. They will mature May 15, 2010, but may be redeemed at the option of the United States on and after May 15, 2005, in whole or in part, at par and accrued interest on any interest payment date or dates, on 4 months' notice of call given in such manner as the Secretary of the Treasury shall prescribe. In case of partial call, the securities to be redeemed will be determined by such method as may be prescribed by the Secretary of the Treasury. Interest on the securities called for redemption shall cease on the date of redemption specified in the notice of call.

2.2. The income derived from the securities is subject to all taxes imposed under the Internal Revenue Code of 1954. The securities are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, any possession of the United States, or any local taxing authority.

2.3. The securities will be acceptable to secure deposits of public monies. They will not be acceptable in payment of taxes.

2.4. Bearer securities with interest coupons attached, and securities registered as to principal and interest, will be issued in denominations of \$1,000, \$5,000, \$10,000, \$100,000, and \$1,000,000. Book-entry securities will be available to eligible bidders in multiples of those amounts. Interchanges of securities of different denominations and of coupon, registered and book-entry securities, and the transfer of registered securities will be permitted.

2.5. The Department of the Treasury's general regulations governing United States securities apply to the securities offered in this circular. These general regulations include those currently in effect, as well as those that may be issued at a later date.

### 3. SALE PROCEDURES

3.1. Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Daylight Saving time, Thursday, May 8, 1980. Noncompetitive tenders as defined below will be considered timely if postmarked no later than Wednesday, May 7, 1980.

3.2. Each tender must state the face amount of securities bid for. The minimum bid is \$1,000 and larger bids must be in multiples of that amount. Competitive tenders must also show the yield desired, expressed in terms of an annual yield with two decimals, e.g., 7.11%. Common fractions may not be used. Noncompetitive tenders must show the term "noncompetitive" on the tender form in lieu of a specified yield. No bidder may submit more than one noncompetitive tender and the amount may not exceed \$1,000,000.

3.3. All bidders must certify that they have not made and will not make any agreements for the sale or purchase of any securities of this issue prior to the deadline established in Section 3.1. for receipt of tenders. Those authorized to submit tenders for the account of customers will be required to certify that such tenders are submitted under the same conditions, agreements, and certifications as tenders submitted directly by bidders for their own account.

3.4. Commercial banks, which for this purpose are defined as banks accepting demand deposits, and primary dealers, which for this purpose are defined as dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, may submit tenders for account of customers if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account.

3.5. Tenders will be received without deposit for their own account from commercial banks and other banking institutions; primary dealers, as defined above; Federally-insured savings and loan associations; States, and their political subdivisions or instrumentalities; public pension and retirement and other public funds; international organizations in which the United States holds membership; foreign central banks and foreign states; Federal Reserve Banks; and Government accounts. Tenders from others must be accompanied by full payment for the amount of securities applied for (in the form of cash, maturing Treasury securities or readily collectible checks), or by a payment guarantee of 5 percent of the face amount applied for, from a commercial bank or a primary dealer.

3.6. Immediately after the closing hour, tenders will be opened, followed by a public announcement of the amount and yield range of accepted bids. Subject to the reservations expressed in Section 4, noncompetitive tenders will be accepted in full, and then competitive tenders will be accepted, starting with those at the lowest yields, through successively higher yields to the extent required to attain the amount offered. Tenders at the highest accepted yield will be prorated if necessary. After the determination is made as to which tenders are accepted, a coupon rate will be established, on the basis of a  $\frac{1}{8}$  of one percent increment, which results in an equivalent average accepted price close to 100.000 and a lowest accepted price above the original issue discount limit of 92.500. That rate of interest will be paid on all of the securities. Based on such interest rate, the price on each competitive tender allotted will be determined and each successful competitive bidder will be required to pay the price equivalent to the yield bid. Those submitting noncompetitive tenders will pay the price equivalent to the weighted average yield of accepted competitive tenders. Price calculations will be carried to three decimal places on the basis of price per hundred, e.g., 99.923, and the determinations of the Secretary of the Treasury shall be final. If the amount of noncompetitive tenders received would absorb all or most of the offering, competitive tenders will be accepted in an amount sufficient to provide a fair determination of the yield. Tenders received from Government accounts and Federal Reserve Banks will be accepted at the price equivalent to the weighted average yield of accepted competitive tenders.

3.7. Competitive bidders will be advised of the acceptance or rejection of their tenders. Those submitting noncompetitive tenders will only be notified if the tender is not accepted in full, or when the price is over par.



#### 4. RESERVATIONS

4.1. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders in whole or in part, to allot more or less than the amount of securities specified in Section 1, and to make different percentage allotments to various classes of applicants when the Secretary considers it in the public interest. The Secretary's action under this Section is final.

#### 5. PAYMENT AND DELIVERY

5.1. Settlement for allotted securities must be made at the Federal Reserve Bank or Branch or at the Bureau of the Public Debt, wherever the tender was submitted. Settlement on securities allotted to institutional investors and to other whose tenders are accompanied by a payment guarantee as provided in Section 3.5., must be made or completed on or before Thursday, May 15, 1980. Payment in full must accompany tenders submitted by all other investors. Payment must be in cash; in other funds immediately available to the Treasury; in Treasury bills, notes or bonds (with all coupons detached) maturing on or before the settlement date but which are not overdue as defined in the general regulations governing United States securities; or by readily collectible check drawn to the order of the institution to which the tender was submitted, which must be received at such institution no later than Monday, May 12, 1980. When payment has been submitted with the tender and the purchase price of allotted securities is over par, settlement for the premium must be completed timely, as specified in the preceding sentence. When payment has been submitted with the tender and the purchase price of allotted securities is under par, the discount will be remitted to the bidder. Settlement will not be considered complete where registered securities are requested if the appropriate identifying number as required on tax returns and other documents submitted to the Internal Revenue Service (an individual's social security number or an employer identification number) is not furnished. When payment is made in securities, a cash adjustment will be made to or required of the bidder for any difference between the face amount of securities presented and the amount payable on the securities allotted.

5.2. In every case where full payment is not completed on time, an amount of up to 5 percent of the face amount of securities allotted, shall, at the discretion of the Secretary of the Treasury, be forfeited to the United States.

5.3. Registered securities tendered in payment for allotted securities are not required to be assigned if the new securities are to be registered in the same names and forms as appear in the registrations or assignments of the securities surrendered. When the new securities are to be registered in names and forms different from those in the inscriptions or assignments of the securities presented, the assignment should be to "The Secretary of the Treasury for (securities offered by this circular) in the name of (name and taxpayer identifying number)." If new securities in coupon form are desired, the assignment should be to "The Secretary of the Treasury for coupon (securities offered by this circular) to be delivered to (name and address)." Specific instructions for the issuance and delivery of the new securities, signed by the owner or authorized representative, must accompany the securities presented. Securities tendered in payment should be surrendered to the Federal Reserve Bank or Branch or to the Bureau of the Public Debt, Washington, D. C. 20226. The securities must be delivered at the expense and risk of the holder.

5.4. If bearer securities are not ready for delivery on the settlement date, purchasers may elect to receive interim certificates. These certificates shall be issued in bearer form and shall be exchangeable for definitive securities of this issue, when such securities are available, at any Federal Reserve Bank or Branch or at the Bureau of the Public Debt, Washington, D. C. 20226. The interim certificates must be returned at the risk and expense of the holder.

5.5. Delivery of securities in registered form will be made after the requested form of registration has been validated, the registered interest account has been established, and the securities have been inscribed.

## 6. GENERAL PROVISIONS

6.1. As fiscal agents of the United States, Federal Reserve Banks are authorized and requested to receive tenders, to make allotments as directed by the Secretary of the Treasury, to issue such notices as may be necessary, to receive payment for and make delivery of securities on full-paid allotments, and to issue interim certificates pending delivery of the definitive securities.

6.2. The Secretary of the Treasury may at any time issue supplemental or amendatory rules and regulations governing the offering. Public announcement of such changes will be promptly provided.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

SUPPLEMENT TO DEPARTMENT CIRCULAR NO. 16-80. PUBLIC  
DEBT

DEPARTMENT OF THE TREASURY,  
*Washington, May 9, 1980.*

The Secretary announced on May 8, 1980, that the interest rate on the bonds designated Bonds of 2005-2010, described in Department Circular—Public Debt Series—No. 16-80, dated May 1, 1980, will be 10 percent. Interest on the bonds will be payable at the rate of 10 percent per annum.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

## Summary of information pertaining to Treasury bonds issued during fiscal year 1980

Date of prelim- inary announce- ment	Department circular		Concurrent offering circular No.	Treasury bonds issued (all auctioned for cash)	Type of auction <sup>1</sup>	Accepted tenders			Issue date	Maturity date	Date tenders received
	No.	Date				Average price	High price	Low price			
1978											
Sept. 28	23-79	Oct. 1	.....	10%	.....	99.620	99.013	99.013	Oct. 16	Nov. 15, 1994	Oct. 11
Oct. 24	27-79	Oct. 25	25-79, 26-79	10%	.....	99.407	99.863	99.045	Nov. 15	Nov. 15, 2009	Nov. 1
1979											
Dec. 28	32-79	Dec. 28	.....	10½	.....	99.204	99.352	99.130	Jan. 10	Feb. 15, 1995	Jan. 3
1979											
Jan. 30	7-80	Jan. 31	6-80	11%	.....	99.264	99.754	99.021	Feb. 15	Feb. 15, 2010	Feb. 7
Mar. 20	12-80	Mar. 21	.....	12%	.....	99.492	100.092	99.293	Apr. 8	May 15, 1995	Apr. 2
Apr. 30	16-80	May 1	14-80	10	.....	98.876	99.248	98.322	May 15	May 15, 2010	May 8
June 26	21-80	June 27	.....	10%	.....	99.664	99.813	99.515	July 9	May 15, 1995	July 2
July 30	25-80	July 31	24-80	10%	.....	96.91	97.40	96.18	Aug. 15 <sup>4</sup>	Nov. 15, 2009	Aug. 7

<sup>1</sup> One issue of bonds was auctioned by the "price" method, with the interest rate being announced prior to the auction, and bidders were required to bid at a price. Other auctions were held by the "yield" method in which case bidders were required to bid at a yield. After tenders were allotted in the "yield" method auction, an interest rate for the bonds was established at the nearest one-eighth of 1 percent increment that translated into an average accepted price close to 100.000.

<sup>2</sup> Payment could not be made through Treasury tax and loan accounts for any of the issues.

<sup>3</sup> Relatively small amounts of bids were allotted at a price or prices above the high shown. However, the higher price or prices are not shown in order to prevent an appreciable discontinuity in the range of prices, which would make it misrepresentative.

<sup>4</sup> Interest was payable from Aug. 15, 1980.

NOTE.—The maximum amount that could be bid for on a noncompetitive basis for each issue was \$1 million. All issues had a minimum denomination of \$1,000.



### Exhibit 3.—Treasury bills

During the fiscal year there were 52 weekly issues of 13-week and 26-week bills (the 13-week bills represent additional amounts of bills with an original maturity of 26 weeks), 13 52-week issues, and several issues of cash management bills. A press release inviting tenders for 13-week, 26-week, and 52-week bills is reproduced in this exhibit and is representative of all releases except those for cash management bills. The offering press release of May 23, 1980, inviting tenders for 19-day bills is also included and is representative of all such releases. Also reproduced is a press release which is representative of releases announcing the results of offerings. Data for each issue during the fiscal year appears in table 39 in the Statistical Appendix.

#### PRESS RELEASE OF JULY 15, 1980

##### TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately \$8,000 million, to be issued July 24, 1980. This offering will provide \$1,200 million of new cash for the Treasury as the maturing bills are outstanding in the amount of \$6,796 million, including \$1,166 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and \$1,661 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately \$4,000 million, representing an additional amount of bills dated April 24, 1980, and to mature October 23, 1980 (CUSIP No. 912793 5L 6), originally issued in the amount of \$3,560 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately \$4,000 million to be dated July 24, 1980, and to mature January 22, 1981 (CUSIP No. 912793 6D 3).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing July 24, 1980. Tenders from Federal Reserve Banks for themselves and as agents of foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents of foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of \$10,000 and in any higher \$5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Daylight Saving time, Monday, July 21, 1980. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of \$10,000. Tenders over \$10,000 must be in multiples of \$5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with not more than three decimals, e.g., 99.925. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of \$200 million. This information should reflect positions held at the close of business on the day prior to the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering; e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary

markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds \$200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for \$500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on July 24, 1980, in cash or other immediately available funds or in Treasury bills maturing July 24, 1980; provided, however, that settlement for tenders submitted to the Federal Reserve Bank Branch in Salt Lake City must be completed at that Branch on July 25, 1980, and must include one day's accrued interest if settlement is made with other than Treasury bills maturing July 24, 1980. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

Under Sections 454(b) and 1221(5) of the Internal Revenue Code of 1954 the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed or otherwise disposed of, and the bills are excluded from consideration as capital assets. Accordingly, the owner of these bills (other than life insurance companies) must include in his or her Federal income tax return, as ordinary gain or loss, the difference between the price paid for the bills, whether on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made.

Department of the Treasury Circulars, Public Debt Series—Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

## PRESS RELEASE OF JULY 10, 1980

### TREASURY'S 52-WEEK BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for approximately \$4,000 million, of 359-day Treasury bills to be dated July 22, 1980, and to mature July 16, 1981 (CUSIP No. 912793 6W 1). This issue will provide about \$600 million new cash for the Treasury as the maturing issue is outstanding in the amount of \$3,389 million, including \$634 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and \$975 million currently held by Federal Reserve Banks for their own account.

The bills will be issued for cash and in exchange for Treasury bills maturing July 22, 1980. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average price of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to

the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. This series of bills will be issued entirely in book-entry form in a minimum amount of \$10,000 and in any higher \$5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Daylight Saving time, Wednesday, July 16, 1980. Form PD 4632-1 should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of \$10,000. Tenders over \$10,000 must be in multiples of \$5,000. In the case of competitive tenders, the price offered must be expressed on the basis of 100, with not more than three decimals, e.g., 99.925. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of \$200 million. This information should reflect positions held at the close of business on the day prior to the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds \$200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for \$500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on July 22, 1980, in cash or other immediately available funds or in Treasury bills maturing July 22, 1980. Cash adjustments will be made for differences between the par value of maturing bills accepted in exchange and the issue price of the new bills.

### PRESS RELEASE OF MAY 23, 1980

#### TREASURY OFFERS \$2,700 MILLION OF 19-DAY CASH MANAGEMENT BILLS

The Department of the Treasury, by this public notice, invites tenders for approximately \$2,700 million of 19-day Treasury bills to be issued May 29, 1980, and maturing June 17, 1980 (CUSIP No. 912793 7C 4). Additional amounts of the bills may



be issued to Federal Reserve Banks as agents for foreign and international monetary authorities at the average price of accepted competitive tenders.

Competitive tenders will be received at all Federal Reserve Banks and Branches up to 1:30 p.m., Eastern Daylight Saving time, Tuesday, May 27, 1980. Wire and telephone tenders may be received at the discretion of each Federal Reserve Bank or Branch. Each tender for the issue must be for a minimum amount of \$10,000,000. Tenders over \$10,000,000 must be in multiples of \$1,000,000. The price on tenders offered must be expressed on the basis of 100, with not more than three decimals, e.g., 99.925. Fractions may not be used.

Noncompetitive tenders from the public will not be accepted. Tenders will not be received at the Department of the Treasury, Washington.

The bills will be issued on a discount basis under competitive bidding, and at maturity their par amount will be payable without interest. The bills will be issued entirely in book-entry form in a minimum denomination of \$10,000 and in any higher \$5,000 multiple, on the records of the Federal Reserve Banks and Branches.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of \$200 million. This information should reflect positions held at the close of business on the day prior to the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering; e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds \$200 million.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank or Branch in cash or other immediately available funds on Thursday, May 29, 1980.

Under Sections 454(b) and 1221(5) of the Internal Revenue Code of 1954 the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed or otherwise disposed of, and the bills are excluded from consideration as capital assets. Accordingly, the owner of these bills (other than life insurance companies) must include in his or her Federal income tax return, as ordinary gain or loss, the difference between the price paid for the bills on original issue or on subsequent purchase, and the amount actually received either upon sale or redemption at maturity during the taxable year for which the return is made.

Department of the Treasury Circulars, No. 418 (current revision), Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars may be obtained from any Federal Reserve Bank or Branch.

## PRESS RELEASE OF JUNE 2, 1980

### RESULT OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for \$3,601 million of 13-week bills and for \$3,600 million of 26-week bills, both to be issued on June 5, 1980, were accepted today.

*Range of accepted competitive bids*

	13-week bills maturing Sept. 4, 1980			26-week bills maturing Dec. 4, 1980		
	Price	Discount rate	Investment rate <sup>1</sup>	Price	Discount rate	Investment rate <sup>1</sup>
High .....	98.003	7.900%	8.17%	95.914	8.082%	8.54%
Low .....	97.957	8.082%	8.37%	95.844	8.221%	8.70%
Average .....	97.969	8.035%	8.32%	95.872	8.165%	8.64%

<sup>1</sup>Equivalent coupon-issue yield.

NOTE.—Tenders at the low price for the 13-week bills were allotted 30 percent.

—Tenders at the low price for the 26-week bills were allotted 44 percent.

*Tenders received and accepted*  
[In thousands]

	Received	Accepted	Received	Accepted
Location:				
Boston .....	\$70,160	\$32,160	\$50,570	\$30,570
New York .....	5,209,305	2,894,305	4,798,720	2,975,800
Philadelphia .....	23,860	23,860	13,785	13,785
Cleveland .....	90,575	40,575	35,475	15,475
Richmond .....	29,990	29,990	48,580	41,580
Atlanta .....	49,120	47,120	20,985	20,985
Chicago .....	458,500	173,500	395,335	197,935
St. Louis .....	56,170	32,170	42,770	20,650
Minneapolis .....	15,550	15,550	11,380	11,380
Kansas City .....	37,530	37,530	19,535	19,535
Dallas .....	15,890	15,890	8,050	8,050
San Francisco .....	362,710	167,710	298,525	171,725
Treasury .....	90,870	90,850	72,720	72,720
Total .....	6,510,230	3,601,210	5,816,430	3,600,190
Type:				
Competitive .....	4,586,830	1,677,810	4,323,020	2,106,780
Noncompetitive .....	618,520	618,520	301,570	301,570
Subtotal, public .....	5,205,350	2,296,330	4,624,590	2,408,350
Federal Reserve .....	900,000	900,000	898,650	898,650
Foreign official institutions .....	404,880	404,880	293,190	293,190
Total .....	6,510,230	3,601,210	5,816,430	3,600,190

NOTE.—An additional \$257,320,000 of 13-week bills and an additional \$191,100,000 of 26-week bills will be issued to foreign official institutions for new cash.

**Exhibit 4.—Department Circular No. 1-80, offering of United States savings bonds, Series EE**

DEPARTMENT OF THE TREASURY,  
*Washington, December 7, 1979.*

**SUMMARY:** This circular contains the terms and conditions of the offering of United States savings bonds of Series EE. These bonds will be offered for sale as of January 1, 1980. United States savings bonds of Series E are being withdrawn from sale. Their over-the-counter sale will be terminated as of December 31, 1979, and issues under payroll savings plans will be terminated as of June 30, 1980.

**EFFECTIVE DATE:** January 1, 1980.

**SUPPLEMENTARY INFORMATION:** For the most part, Series EE bonds resemble and are patterned after bonds of Series E. There are, however, several significant differences between the two series.

Series EE bonds will be identified as Energy Savings Bonds. An energy bonus of one-half of one percent is being offered on each Series EE bond that is held until maturity. This bonus becomes fixed as a part of the maturity value and is payable upon redemption at or after maturity. It increases the effective yield on bonds held to maturity to 7 percent.

The issue price of a Series EE bond is 50 percent of the face amount, whereas the Series E bond sold at 75 percent of face amount.

The term of the Series EE bond is 11 years, in contrast to the 5-year term of Series E bonds. However, the yield on both series is 6 ½ percent, compounded semiannually, if the bonds are held for a minimum of 5 years. The energy bonus raises the yield on bonds held for 11 years.

The Series EE bond denominations do not include a \$25 bond. The smallest denomination is \$50, for which the issue price is \$25.

Series EE bonds are eligible for redemption after six months, whereas Series E bonds are eligible after two months. This change will improve the cost effectiveness of the Savings Bond Program.

Series EE bonds may be exchanged for Series HH bonds at any time after six months from issue.

The annual limitation on purchases of Series EE bonds is \$30,000 (face amount), an increase over the annual limitation for Series E bonds.

The regulations (Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR, Part 353)) provide that the consent of the beneficiary is not required for the reissue of Series EE bonds in beneficiary form.

The Secretary of the Treasury hereby makes the following offering of the United States Savings Bonds of Series EE, which is Part 351 of Title 31, Code of Federal Regulations.

Since this offering involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary.

A new Part 351 is added to read as set forth below:

**PART 351-OFFERING OF UNITED STATES SAVINGS BONDS, SERIES EE**

**§ 351.0 Offering of bonds.**

The Secretary of the Treasury offers for sale to the people of the United States, United States Savings Bonds of Series EE, hereinafter referred to as "Series EE bonds" or "bonds." This offer, effective as of January 1, 1980, will continue until terminated by the Secretary of the Treasury.

**§ 351.1 Governing regulations.**

Series EE bonds are subject to the regulations of the Department of the Treasury, now or hereafter prescribed, governing United States Savings Bonds of Series EE and HH, contained in Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR Part 353), hereinafter referred to as Circular No. 3-80.



### § 351.2 Description of bonds.

(a) *General.* Series EE bonds are issued only in registered form and are nontransferable.

(b) *Denominations and prices.* Series EE bonds are issued on a discount basis. The denominations and issue prices are:

<i>Denomination:</i>	<i>Issue price</i>
\$50.....	\$25.00
\$75.....	\$37.50
\$100.....	\$50.00
\$200.....	\$100.00
\$500.....	\$250.00
\$1,000.....	\$500.00
\$5,000.....	\$2,500.00
\$10,000.....	\$5,000.00

(c) *Term.* The issue date of a Series EE bond is the first day of the month in which payment of the issue price is received by an authorized issuing agent. The bond matures 11 years from its issue date.

(d) *Redemption.* A Series EE bond may be redeemed after six months from issue date at fixed redemption values. See Table 1. The Secretary of the Treasury may not call Series EE bonds for redemption prior to maturity.

(e) *Interest (investment yield).*—(1) *Rate of interest.* The investment yield (interest) is approximately 6 ½ percent per annum, compounded semiannually, if the bond is held for a minimum of five years. The yield is less if the bond is redeemed earlier.

(2) *Energy bonus.* An energy bonus of one-half of one percent will be added to the redemption value of any Series EE bond held to maturity. With the bonus, the overall investment yield will be approximately 7 percent per annum, compounded semiannually.

(3) *Accrual and payment of interest.* Interest accrues on a Series EE bond and becomes a part of the redemption value which is paid when the bond is cashed. The redemption value of a bond increases on the first day of each month from the third through the thirtieth month after issue, and thereafter on the first day of each successive six-month period. The interest on outstanding bonds ceases to accrue after final maturity.

### § 351.3 Registration and issue.

(a) *Registration.* Bonds may be registered in the names of natural persons in single ownership, coownership, or beneficiary form. Bonds may also be registered in the names of organizations and fiduciaries. Specific rules and examples are contained in Subpart B of Circular No. 3-80.

(b) *Validity of issue.* A bond is validly issued when it (1) is registered as provided in Circular No. 3-80; and (2) bears an issue date and the validation indicia of an authorized issuing agent.

(c) *Taxpayer identifying number.* The inscription of a bond must include the taxpayer identifying number of the owner or first-named co-owner. The taxpayer identifying number of the second-named co-owner or beneficiary is not required but its inclusion is desirable. If the bond is being purchased as a gift or award and the owner's taxpayer identifying number is not known, the taxpayer identifying number of the purchaser and the word "GIFT" must be included in the inscription.

(d) *Restrictions on chain letters.* The issuance of bonds in the furtherance of a chain letter or pyramid scheme is considered to be against the public interest and is prohibited. An issuing agent is authorized to refuse to issue a bond if there is reason to believe that the purchase is in connection with a chain letter and its decision is final.

### § 351.4 Limitation on purchases.

The amount of Series EE bonds which may be purchased and held in the name of any one person in any one calendar year is limited to \$30,000 (face amount). Subpart C of Circular No. 3-80 contains the rules governing the computation of amounts and the special limitation for employee plans.

### § 351.5 Purchase of bonds.

(a) *Payroll plans.* Bonds may be purchased through deductions from the pay of employees of organizations which maintain payroll savings plans. The bonds must be issued by an authorized issuing agent, which may be the employer organization or a financial institution or the Federal Reserve Bank or Branch servicing that organization.

(b) *Over-the-counter/mail.*—(1) *At financial institutions.* Bonds registered in the names of individuals in their own right may be purchased over-the-counter or by mail from any financial institution, i.e., bank, savings and loan association, etc., qualified as an issuing agent.

(2) *At Federal Reserve Banks or Branches and the Bureau of the Public Debt.*—(i) *General.* Bonds registered in any authorized form may be purchased over-the-counter or by mail from a Federal Reserve Bank or Branch, and from the Bureau of the Public Debt, Washington, D.C. 20226.

(ii) *Remittance.* The application for purchase of a bond from a Federal Reserve Bank or Branch or from the Bureau of the Public Debt, Washington, D.C. 20226, must be accompanied by the remittance to cover the issue price. Checks or other forms of exchange, which will be accepted subject to collection, should be drawn to the order of the Federal Reserve Bank or the Bureau of the Public Debt, as the case may be. Checks payable by endorsement are not acceptable.

(3) *Payment with savings stamps.* Savings stamps will be accepted in payment for Series EE bonds purchased over-the-counter or by mail.

(c) *Bond-a-month plan.* A depositor of a financial institution qualified as an issuing agent may purchase bonds through a system of regular monthly withdrawals from the depositor's account.

(d) *Employee thrift, savings, vacation, and similar plans.* Bonds registered in the names of trustees of employee plans may be purchased either (1) from a Federal Reserve Bank or Branch, or (2) from a financial institution which:

(i) Is a qualified issuing agent;

(ii) Has been designated trustee of an approved employee plan eligible for the special limitation under § 353.13 of Circular No. 3-80; and

(iii) Has obtained prior approval to issue the bonds from the Federal Reserve Bank of the agent's district.

### § 351.6 Delivery of bonds.

Issuing agents are authorized to deliver Series EE bonds either over-the-counter or by mail. Mail deliveries are made at the risk and expense of the United States to the address given by the purchaser, if it is within the United States, its territories or possessions, or the Commonwealth of Puerto Rico. No mail deliveries elsewhere will be made, except to residents of Mexico and Canada who participate in payroll savings plans and to residents of what was formerly the Panama Canal Zone. Bonds purchased by a citizen of the United States residing abroad will be delivered only to such address in the United States as the purchaser directs.

### § 351.7 Payment or redemption.

(a) *Incorporated banks, savings and loan associations, and other financial institutions.* A financial institution qualified as a paying agent under the provisions of Department of the Treasury Circular No. 750 (31 CFR Part 321), will pay the current redemption value of a Series EE bond presented for payment by an individual whose name is inscribed on the bond as owner or co-owner, provided: (1) The bond is in order for payment and (2) the presenter establishes his or her identity to the satisfaction of the agent, in accordance with Treasury instructions and identification guidelines, and signs and completes the request for payment.

(b) *Federal Reserve Bank and Branches and the Bureau of the Public Debt.* A Federal Reserve Bank or Branch or the Bureau of the Public Debt will pay the current redemption value of a Series EE bond presented for payment, provided the bond is in order for payment and the request for payment is properly signed and certified in accordance with Circular No. 3-80.

### § 351.8 Taxation.

(a) *General.* The increment in value, represented by the difference between the price paid for a Series EE bond and the redemption value received for it, is interest. This interest is subject to all taxes imposed under the Internal Revenue Code of 1954, as amended. The bonds are subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but are exempt from all other taxation now or hereafter imposed on the principal or interest by any State, any possession of the United States or any local taxing authority.

(b) *Federal income tax on bonds.* The owner of a Series EE bond may use either of the following two methods for reporting the increase in the redemption value of the bond for Federal income tax purposes:

(1) *Cash basis.* Defer reporting the increase to the year of final maturity, redemption, or other disposition, whichever is earlier; or

(2) *Accrual basis.* Elect to report the increase each year as it accrues, in which case the election applies to all Series EE bonds then owned by the taxpayer and those subsequently acquired, as well as to any other obligations purchased on a discount basis, such as those of Series E.

If the method in paragraph (b)(1) of this section is used, the taxpayer may change to the method in paragraph (b)(2) of this section without obtaining permission from the Internal Revenue Service. However, once the election to use the method in paragraph (b)(2) of this section is made, the taxpayer may not change the method of reporting unless he or she obtains permission from the Internal Revenue Service. For further information, the District Director of the taxpayer's district, or the Internal Revenue Service, Washington, D.C. 20224, should be consulted.

(c) *Tax-deferred exchanges.* Department of the Treasury Circular, Public Debt Series No. 2-80 (31 CFR Part 352), authorizes the exchange of Series EE bonds for Series HH bonds with a continuation of the tax-deferral privilege. The rules governing tax-deferred exchanges are contained in that Circular.

(d) *Reissue.* A reissue that affects the rights of any of the persons named on a Series EE bond may have a tax consequence.

### § 351.9 Reservation as to issue of bonds.

The Commissioner of the Public Debt, as delegate of the Secretary of the Treasury, is authorized to reject any application for Series EE bonds, in whole or in part, and to refuse to issue or permit to be issued any bonds in any case or class of cases, if he deems the action to be in the public interest, and his action in any such respect is final.

### § 351.10 Waiver.

The Commissioner of the Public Debt, as delegate of the Secretary of the Treasury, may waive or modify any provision of this circular in any particular case or class of cases for the convenience of the United States or in order to relieve any person or persons of unnecessary hardship (a) if such action would not be inconsistent with law or equity, (b) if it does not impair any existing rights, and (c) if he is satisfied that such action would not subject the United States to any substantial expense or liability.

### § 351.11 Fiscal agents.

Federal Reserve Banks and Branches, as fiscal agents of the United States, are authorized to perform such services as may be requested of them by the Secretary of the Treasury, or his delegate, in connection with the issue, servicing and redemption of Series EE bonds.



EE bonds bearing issue dates beginning January 1, 1980

Issue price Maturity value	Period (years and months after issue)	(1) Redemption values during each period first day of period					(2) From issue date to start of period		(3) During each period		(4) From start of period to maturity	
		\$25.00	\$37.50	\$50.00	\$100.00	\$250.00	\$500.00	\$2500.00	\$5000.00	Percent	Percent	Percent
\$25.00		\$25.00	\$37.50	\$50.00	\$100.00	\$250.00	\$500.00	\$2500.00	\$5000.00	—	4.35	7.00
53.28		53.28	79.92	106.56	213.12	532.80	1065.60	5328.00	10656.00	4.35	3.84	7.04
	0-0 to 0-2	25.18	37.77	50.36	100.72	251.80	503.60	2518.00	5036.00	4.18	3.83	7.06
	0-2 to 0-3	25.26	37.89	50.52	101.04	252.60	505.20	2526.00	5052.00	4.09	3.82	7.09
	0-3 to 0-4	25.34	38.01	50.68	101.36	253.40	506.80	2534.00	5068.00	4.04	3.81	7.12
	0-4 to 0-5	25.42	38.13	50.84	101.68	254.20	508.40	2542.00	5084.00	4.00	4.75	7.14
	0-5 to 0-6	25.50	38.25	51.00	102.00	255.00	510.00	2550.00	5100.00	4.11	4.73	7.16
	0-6 to 0-7	25.60	38.40	51.20	102.40	256.00	512.00	2560.00	5120.00	4.19	5.67	7.18
	0-7 to 0-8	25.70	38.55	51.40	102.80	257.00	514.00	2570.00	5140.00	4.35	5.64	7.19
	0-8 to 0-9	25.82	38.73	51.64	103.28	258.20	516.40	2582.00	5164.00	4.48	4.67	7.21
	0-9 to 0-10	25.94	38.91	51.88	103.76	259.40	518.80	2594.00	5188.00	4.50	4.65	7.23
	0-10 to 0-11	26.04	39.06	52.08	104.16	260.40	520.80	2604.00	5208.00	4.51	5.57	7.25
	0-11 to 0-0	26.14	39.21	52.28	104.56	261.40	522.80	2614.00	5228.00	4.59	4.61	7.26
	1-0 to 1-1	26.26	39.39	52.52	105.04	262.60	525.20	2626.00	5252.00	4.50	4.60	7.29
	1-1 to 1-2	26.36	39.54	52.72	105.44	263.60	527.20	2636.00	5272.00	4.50	5.50	7.31
	1-2 to 1-3	26.46	39.69	52.92	105.84	264.60	529.20	2646.00	5292.00	4.65	5.48	7.32
	1-3 to 1-4	26.58	39.87	53.16	106.32	265.80	531.60	2658.00	5316.00	4.70	4.54	7.34
	1-4 to 1-5	26.70	40.05	53.40	106.80	267.00	534.00	2670.00	5340.00	4.69	4.52	7.37
	1-5 to 1-6	26.80	40.20	53.60	107.20	268.00	536.00	2680.00	5360.00	4.68	5.41	7.39
	1-6 to 1-7	26.90	40.35	53.80	107.80	269.00	538.00	2690.00	5380.00	4.72	5.39	7.43
	1-7 to 1-8	27.02	40.53	54.04	108.08	270.20	540.40	2702.00	5404.00	4.75	5.34	7.45
	1-8 to 1-9	27.14	40.71	54.28	108.56	271.40	542.80	2714.00	5428.00	4.74	5.43	7.47
	1-9 to 1-10	27.24	40.86	54.48	108.96	272.40	544.80	2724.00	5448.00	4.76	4.43	7.47
	1-10 to 1-11	27.36	41.04	54.72	109.44	273.60	547.20	2736.00	5472.00	4.77	5.30	7.50
	1-11 to 1-0	27.46	41.19	54.92	109.84	274.60	549.20	2746.00	5492.00	4.79	5.28	7.52
	2-0 to 2-1	27.58	41.37	55.16	110.32	275.80	551.60	2758.00	5516.00	4.82	5.26	7.54
	2-1 to 2-2	27.7-	41.55	55.40	110.80	277.00	554.00	2770.00	5540.00	4.81	5.23	7.57
	2-2 to 2-3	27.82	41.73	55.64	111.28	278.20	556.40	2782.00	5564.00	4.82	5.21	7.59
	2-3 to 2-4	27.94	41.91	55.88	111.76	279.40	558.80	2794.00	5588.00	4.84	5.19	7.61
	2-4 to 2-5	28.06	42.09	56.12	112.24	280.60	561.20	2806.00	5612.00	4.85	5.39	7.64
	2-5 to 2-6	28.18	42.27	56.36	112.72	281.80	563.60	2818.00	5636.00	4.94	5.53	7.78
	2-6 to 3-0	28.30	42.45	56.60	113.20	283.00	566.00	2830.00	5660.00	4.94	5.53	7.78
	3-0 to 3-6	28.94	43.41	57.88	115.76	289.40	578.80	2894.00	5788.00	4.94	5.53	7.78

## EE bonds bearing issue dates beginning January 1, 1980—Continued

Issue price .....	\$25.00	\$37.50	\$50.00	\$100.00	\$250.00	\$500.00	\$2500.00	\$5000.00	Approximate investment yield (annual percentage rate)			
									(2) From issue date to start of period	(3) During each period	(4) From start of period to maturity	Percent
Maturity value.....	53.28	79.92	106.56	213.12	532.80	1065.60	5328.00	10656.00				
Period (years and months after issue)	(1) Redemption values during each period (values increase on first day of period)											
3- 6 to 4- 0 .....	29.74	44.61	59.48	118.96	297.40	594.80	2974.00	5948.00	Percent	Percent	Percent	Percent
4- 0 to 4- 6 .....	30.84	46.26	61.68	123.36	308.40	616.80	3084.00	6168.00	5.02	7.40	7.93	7.93
4- 6 to 5- 0 .....	32.34	48.51	64.68	129.36	323.40	646.80	3234.00	6468.00	5.32	9.73	7.97	7.97
5- 0 to 5- 6 .....	34.42	51.63	68.84	137.68	344.20	688.40	3442.00	6884.00	5.80	12.86	7.83	7.83
5- 6 to 6- 0 .....	35.54	53.31	71.08	142.16	355.40	710.80	3554.00	7108.00	6.50	6.51	7.42	7.42
6- 0 to 6- 6 .....	36.70	55.05	73.40	146.80	367.00	734.00	3670.00	7340.00	6.50	6.53	7.50	7.50
6- 6 to 7- 0 .....	37.88	56.82	75.76	151.52	378.80	757.60	3788.00	7576.00	6.50	6.43	7.60	7.60
7- 0 to 7- 6 .....	39.12	58.68	78.24	156.48	391.20	782.40	3912.00	7824.00	6.50	6.55	7.73	7.73
7- 6 to 8- 0 .....	40.40	60.60	80.80	161.60	404.00	808.00	4040.00	8080.00	6.50	6.54	7.87	7.87
8- 0 to 8- 6 .....	41.70	62.55	83.40	166.80	417.00	834.00	4170.00	8340.00	6.50	6.44	8.06	8.06
8- 6 to 9- 0 .....	43.06	64.59	86.12	172.24	430.60	861.20	4306.00	8612.00	6.50	6.52	8.34	8.34
9- 0 to 9- 6 .....	44.46	66.69	88.92	177.84	444.60	889.20	4446.00	8892.00	6.50	6.50	8.70	8.70
9- 6 to 10- 0 .....	45.90	68.85	91.80	183.60	459.00	918.00	4590.00	9180.00	6.50	6.48	9.26	9.26
10- 0 to 10- 6 .....	47.40	71.10	94.80	189.60	474.00	948.00	4740.00	9480.00	6.50	6.54	10.19	10.19
10- 6 to 11- 0 .....	48.04	73.41	97.88	195.76	489.40	978.80	4894.00	9788.00	6.50	6.50	12.04	12.04
11- 0 .....	53.28	79.92	106.56	213.12	532.80	1065.60	5328.00	10656.00	6.50	17.74	17.74	17.74

**§ 351.12 Reservation as to terms of offer.**

The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this offering of bonds.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 5.—Department Circular No. 2-80, offering of United States savings bonds, Series HH**

DEPARTMENT OF THE TREASURY,  
*Washington, December 7, 1979.*

**SUMMARY:** This circular contains the terms and conditions of the offering of United States savings bonds of Series HH. These bonds will be offered for sale, as of January 1, 1980. United States savings bonds of Series H are being withdrawn from sale as of December 31, 1979.

**EFFECTIVE DATE:** January 1, 1980.

**SUPPLEMENTARY INFORMATION:** For the most part, Series HH bonds resemble and are patterned after Series H bonds. There are, however, several significant differences between the two series.

As with Series H bonds, Series HH bonds can be purchased for cash and in exchange for accrual-type savings bonds and notes. Provision is also made for purchasing Series HH bonds through the reinvestment of certain matured Series H bonds. There will be two separate, distinguishable types of Series HH bonds, one to identify bonds sold for cash and the other to identify bonds issued on exchange or through reinvestment.

Under the offering, securities eligible for exchange for Series HH bonds are: Series E bonds, until one year after their final maturities; Series EE bonds, beginning six months after their issue; and United States Savings Notes (Freedom Shares). The exchange offer is made a part of the offering circular, rather than being set out in a separate document.

Semiannual interest payments on Series HH bonds are set at uniform amounts for the term to maturity, to eliminate the confusion created by the graduated scale of payments on Series H bonds.

The redemption value of Series HH bonds purchased for cash will be less than the face amount, if the bonds are redeemed within five years of issue. The difference between the face amount and redemption value represents an interest adjustment. The yield is consistent with that of the companion Series EE bonds, which must be held for at least five years to provide a return of 6 ½ percent.

Series HH bonds issued on exchange constitute a continuation of long-term holdings of savings bonds and notes; they are not subject to any interest adjustment.

The registration requirements for a tax-deferred exchange will be the same for Series HH bonds as for Series H bonds. The rules are designed to prevent the shifting of tax liability incident to an exchange. The same requirements apply to non-tax-deferred exchanges for Series HH bonds, even though no tax liability is involved, since the new bonds are not subject to an interest adjustment for early redemption.

As Series H bonds purchased for cash reach final maturity, their proceeds may be reinvested in Series HH bonds. Final maturity dates have been announced for the Series H bonds issued from June 1952 through May 1959, which will become eligible for reinvestment as they mature. All of these bonds were purchased for cash. The reinvestment option will not be available for any Series H bond issued on exchange. The Series HH bonds acquired through reinvestment will not be subject to an interest adjustment.

The annual limitation on cash purchases of Series HH bonds is \$20,000 (face amount), an increase over the \$10,000 limitation for Series H bonds. Bonds issued on exchange or reinvestment are not subject to the annual limitation.



The regulations (Department of the Treasury Circular, Public Debt series No. 3-80 (31 CFR Part 353)) provide that the consent of the beneficiary is not required for the reissue of Series HH bonds in beneficiary form.

The Secretary of the Treasury hereby makes the following offering of United States Savings Bonds of Series HH, which is Part 352 of Title 31, Code of Federal Regulations.

Since this offering involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary.

A new part 352 is added to read as follows:

## PART 352—OFFERING OF UNITED STATES SAVINGS BONDS, SERIES HH

### § 352.0 Offering of bonds.

(a) *Cash offering.* The Secretary of the Treasury offers for sale to the people of the United States, United States Savings Bonds of Series HH, hereinafter referred to as "Series HH bonds" or "bonds" This offer will continue until terminated by the Secretary of the Treasury.

(b) *Exchange offering.* The Secretary of the Treasury also offers to the people of the United States, United States Savings Bonds of Series HH in exchange for outstanding United States Savings Bonds of Series E and EE and United States Savings Notes (Freedom Shares). This offer will continue until terminated by the Secretary of the Treasury.

(c) *Effective date.* These offers are effective as of January 1, 1980. They supersede previous offers of United States Savings Bonds of Series H, contained in Department of the Treasury Circular No. 905 (31 CFR Part 332) and Department of the Treasury Circular No. 1036 (31 CFR Part 339).

### § 352.1 Governing regulations.

Series HH bonds are subject to the regulations of the Department of the Treasury, now or hereafter prescribed, governing United States Savings Bonds of Series EE and HH, contained in Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR Part 353), hereinafter referred to as Circular No. 3-80.

### § 352.2 Description of bonds.

(a) *General.* Series HH bonds are issued only in registered form and are nontransferable. Bonds sold for cash and bonds issued on exchange are distinguishable by: (1) The portraits, color and border design; (2) the tax-deferral legend on the bonds issued on exchange; (3) the word "CASH" or "EXCHANGE," as appropriate, on the back of the bond; and (4) the text material.

(b) *Denominations and prices.* Series HH bonds are issued at face amount and are in denominations of \$500, \$1,000, \$5,000 and \$10,000.

(c) *Term.* Each bond bears an issue date, which is the date from which interest is earned. The date is established, as provided in § 352.7(d) for cash purchases and in § 352.8(e) for exchange issues. The bond matures 10 years from its issue date.

(d) *Redemption—(1) General.* A Series HH bond may be redeemed after six months from its issue date. The Secretary of the Treasury may not call Series HH bonds for redemption prior to maturity. A bond received for redemption by an agent during the calendar month preceding any interest payment date will not ordinarily be paid until that date.

(2) *Bonds purchased for cash.* During the first five years from issue, the redemption value of a bond purchased for cash is less than its face amount. See Table 1. The difference between the face amount and redemption value represents an adjustment of interest. After five years, the bond will be paid at face amount.

(3) *Bonds issued on exchange.* Bonds issued on exchange, including authorized reinvestment, are not subject to an interest adjustment and will be redeemed at face amount at any time after six months from their issue dates.

(e) *Interest (investment yield).* The interest on a Series HH bond is paid semiannually by check drawn to the order of the registered owner or co-owners, beginning six

months from the issue date. The level interest payments will produce a yield of 6 ½ percent per annum, compounded semiannually, on all bonds issued on exchange and on bonds sold for cash that are held for at least five years from their issue. Interest ceases at final maturity or, if the bond is redeemed before final maturity, as of the end of the interest period next preceding the date of redemption. However, if the date of redemption falls on an interest payment date, interest ceases on that date.

### § 352.3 Registration and issue.

(a) *Registration.* Bonds may be registered in the names of natural persons in single ownership, coownership or beneficiary forms. Bonds may also be registered in the names of organizations and fiduciaries. Specific rules and examples are contained in Subpart B of Circular No. 3-80.

(b) *Validity of issue.* A bond is validly issued when it (1) is registered as provided in Circular No. 3-80 and in this circular; and (2) bears an issue date and the validation indicia of an authorized issuing agent.

(c) *Taxpayer identifying number.* The inscription of a bond must include the taxpayer identifying number of the owner or first-named co-owner. The taxpayer identifying number of the second-named co-owner or beneficiary is not required but its inclusion is desirable.

### § 352.4 Limitation on purchases.

The amount of Series HH bonds that may be purchased for cash and held in the name of any one person in any one calendar year is limited to \$20,000 (face amount). Bonds issued on authorized exchange or reinvestment are not subject to this limitation. Subpart C of Circular No. 3-80 contains the rules governing the computation of amounts and the special limitation for exempt organizations.

### § 352.5 Authorized issuing and paying agents.

Series HH bonds may be issued or redeemed only by (a) a Federal Reserve Bank or Branch, (b) the Bureau of the Public Debt, Washington, D.C. 20226, or (c) the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101.

### § 352.6 Cash purchases.

(a) *Basis for issue.* Series HH bonds will be issued by an authorized issuing agent upon receipt of a properly executed application and payment in the form of (1) cash; (2) a check drawn to the order of the Federal Reserve Bank or Branch or the Bureau of the Public Debt; or (3) savings stamps.

(b) *Role of financial institutions.* Financial institutions may submit purchase applications and payment to a Federal Reserve Bank or Branch on behalf of customers.

(c) *Registration.* Bonds may be registered in any authorized form in accordance with Subpart B of Circular No. 3-80.

(d) *Dating.* Bonds will be dated as of the first day of the month in which an authorized issuing agent receives a properly executed purchase application and payment in immediately available funds, or, if payment is made by a financial institution through the Treasury tax and loan account, the first day of the month in which that account is credited.

### § 352.7 Issues on exchange.

(a) *Securities eligible for exchange.* Owners may exchange United States Savings Bonds of Series E and EE and United States Savings Notes (Freedom Shares) at their current redemption values for Series HH bonds. Series E bonds are eligible for exchange until one year after their final maturity dates. Series EE bonds become eligible for exchange six months after their issue dates.

(b) *Basis for issue.* Series HH bonds will be issued on exchange by an authorized issuing agent upon receipt of a properly executed exchange subscription with eligible securities and additional cash, if any, and any supporting evidence that may be required under the regulations. If eligible securities are submitted directly to a Federal Reserve Bank or Branch or the Bureau of the Public Debt, each must bear a properly

signed and certified request for payment. Checks in payment of any cash difference (see paragraph (d) of this section) must be drawn to the order of the Federal Reserve Bank or Branch or Bureau of the Public Debt.

(c) *Role of financial institutions.* Department of the Treasury Circular No. 750, current revision (31 CFR &art 321), authorizes financial institutions qualified as paying agents for savings bonds and notes to redeem eligible securities presented for exchange and to forward an exchange subscription and full payment to a Federal Reserve Bank or Branch for the issue of Series HH bonds. The securities redeemed on exchange by such an institution must be securities which it is authorized to redeem for cash.

(d) *Computation of issue price.* The total current redemption value of the eligible securities submitted in exchange in any one transaction must be \$500 or more. If the current redemption value is an even multiple of \$500, Series HH bonds must be requested in that exact amount. If the total current redemption value exceeds, but is not an even multiple of, \$500, the owner has the option either of furnishing the cash necessary to obtain Series HH bonds at the next highest \$500 multiple, or of receiving payment of the difference between the total current redemption value and the next lower \$500 multiple. For example, if the eligible securities presented for exchange in one transaction have a total current redemption value of \$4,253.33, the owner may elect to:

(1) Receive \$4,000 in Series HH bonds and the amount of the difference, \$253.33; or  
(2) Pay the difference, \$246.67, necessary to obtain \$4,500 in Series HH bonds.

(e) *Registration.* A Series HH bond issued on exchange may be registered in any authorized form (see Subpart B of Circular No. 3-80), subject to the following restrictions:

(1) If the securities submitted in exchange are in single ownership form, the owner must be named as owner or first-named co-owner on the Series HH bonds. A co-owner or beneficiary may be named.

(2) If the securities submitted in exchange are in coownership form, and one coowner is the "principal coowner," the "principal coowner" must be named as owner or first-named coowner. A beneficiary or coowner may also be named. The "principal coowner" is a coowner who (i) purchased the securities submitted for exchange with his or her own funds, or (ii) received them as a gift, inheritance or legacy, or as a result of judicial proceedings, and had them reissued in coownership form, provided he or she has received no contribution in money or money's worth for designating the other coowner on the securities.

(3) If the securities submitted in exchange are in coownership form and both coowners shared in the purchase of the securities or received them jointly as a gift, inheritance or legacy, or as a result of judicial proceedings, both persons must be named as coowners on the Series HH bonds.

(4) If the securities submitted in exchange are in beneficiary form, the owner must be named on the Series HH bonds as owner or first-named coowner. If the owner is deceased, a surviving beneficiary must be named as owner or first-named coowner. In either case, a coowner or beneficiary may be named.

A reissue that affects the rights of any of the persons required to be named on the Series HH bond may have a tax consequence.

(f) *Dating.* Series HH bonds issued on exchange will be dated as of the first day of the month in which the eligible securities presented for exchange are redeemed by a Federal Reserve Bank, the Bureau of the Public Debt, or a qualified paying agent, as evidenced by the payment stamp on the bonds and subscription form.

(g) *Tax-deferred exchanges.* —(1) *Continuation of tax-deferral.* Pursuant to the provisions of Section 1037(a) of the Internal Revenue Code of 1954, as amended, an owner who has not been reporting the interest on his or her Series E or EE savings bonds and savings notes on an accrual basis, for Federal income tax purposes, and who exchanges those securities for Series HH bonds, may continue to defer reporting the interest on the securities exchanged until the taxable year in which the Series HH bonds received in the exchange reach final maturity, are redeemed, or are otherwise disposed of, whichever is earlier.



(2) *Tax-deferral legend.* Each bond issued on a tax-deferred exchange shall bear a legend showing how much of its issue price represents interest on the securities exchanged. This interest must be treated as income for Federal income tax purposes and reported in accordance with paragraph(g)(1) of this section.

(3) *Reporting of interest for any difference paid on exchange.* The amount of any difference paid to the owner (see paragraph (d)(1) of this section) must be treated as income for Federal income tax reporting purposes for the year in which it is received, up to the amount of the total interest on the securities exchanged.

(h) *Exchanges without tax-deferral.* The rules prescribed for exchanges under paragraphs (a) through (f) of this section also apply to exchanges by owners who (1) report the interest on their bonds of Series E and EE and savings notes annually for Federal income tax purposes; (2) elect to report all such interest in the year of the exchange, regardless of whether or not it exceeds the amount of any cash difference received (see paragraph (d)(1) of this section); or (3) are tax-exempt under the provisions of the Internal Revenue Code of 1954, as amended. However, no amount will appear in the tax-deferral legend printed on the bond, and any part of the cash difference received (see paragraph (d)(1) of this section) which represents interest previously reported for Federal income tax purposes need not be treated as income.

#### **§ 352.8 Reinvestment of matured Series H bonds.**

(a) *General.* The face amount of Series H bonds purchased for cash that have reached final maturity may be reinvested in Series HH bonds. The Series H bonds, bearing properly signed and certified requests for payment, must be submitted to a Federal Reserve Bank or Branch or the Bureau of the Public Debt with a reinvestment application.

(b) *Rules.* The reinvestment transaction will be subject to the rules governing exchanges, as set forth in § 352.7, and the Series HH bonds issued on reinvestment will be identical in all respects with those issued on a non-tax-deferred exchange.

#### **§ 352.9 Delivery of bonds.**

Authorized issuing agents will deliver Series HH bonds either (a) over-the-counter, or (b) by mail. Mail deliveries are made at the risk and expense of the United States to the address given by the purchaser, if it is within the United States, one of its territories or possessions, or the Commonwealth of Puerto Rico. No mail deliveries elsewhere will be made. Bonds purchased by a citizen of the United States residing abroad will be delivered only to such address in the United States as the purchaser directs.

#### **§ 352.10 Taxation.**

The interest paid on Series HH bonds is subject to all taxes imposed under the Internal Revenue Code of 1954, as amended. The bonds are subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest by any State, any of the possessions of the United States, or any local taxing authority.

#### **§ 352.11 Reservation as to issue of bonds.**

The Commissioner of the Public Debt, as delegate of the Secretary of the Treasury, is authorized to reject any application for Series HH bonds, in whole or in part, and to refuse to issue or permit to be issued any bonds in any case or class of cases, if he deems the action to be in the public interest, and his action in such respect is final.

#### **§ 352.12 Waiver.**

The Commissioner of the Public Debt, as delegate of the Secretary of the Treasury, may waive or modify any provision of this circular in any particular case or class of cases for the convenience of the United States or in order to relieve any person or persons of unnecessary hardship (a) if such action would not be inconsistent with law

or equity, (b) if it does not impair any existing rights, and (c) if he is satisfied that such action would not subject the United States to any substantial expense or liability.

**§ 352.13 Fiscal agents.**

Federal Reserve Banks and Branches, as fiscal agents of the United States, are authorized to perform such services as may be requested of them by the Secretary of the Treasury, or his delegate, in connection with the issue, servicing and redemption of Series HH bonds.

**§ 352.14 Reservation as to terms of offer.**

The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this offering of bonds.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

H bonds bearing issue dates beginning January 1, 1980, issued in exchange for accrual-type bonds/notes

Issue price .....	\$500.00	\$1,000.00	\$5,000.00	\$10,000.00	Approximate investment yield (annual percentage rate assuming early redemption) *	
					(2) From issue to each interest payment date	(3) For half-year period preceding interest payment date
Maturity value.....	500.00	1,000.00	5,000.00	10,000.00		
Amount of each interest check .....	16.25	32.50	162.50	325.00		
Period of time bond is held after issue date (years and months)	(1) Redemption value of bond					
					Percent	Percent
0-6 to 1-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
1-0 to 1-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
1-6 to 2-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
2-0 to 2-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
2-6 to 3-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
3-0 to 3-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
3-6 to 4-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
4-0 to 4-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
4-6 to 5-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
5-0 to 5-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
5-6 to 6-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
6-0 to 6-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
6-6 to 7-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
7-0 to 7-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
7-6 to 8-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
8-0 to 8-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
8-6 to 9-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
9-0 to 9-6 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
9-6 to 10-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50
10-0 .....	500.00	1000.00	5000.00	10000.00	6.50	6.50

\*The yield from issue to maturity is 6.5 percent.



## HH Bonds bearing issue dates beginning January 1, 1980, purchased by cash

Issue price Maturity value Amount of each interest check ...	\$500.00 500.00 16.25	\$1,000.00 1,000.00 32.50	\$6,000.00 6,000.00 162.50	\$10,000.00 10,000.00 325.00	Approximate investment yield (annual percentage rate assuming early redemption) *			
					(2) From issue to each interest payment date	(3) For half-year period preceding interest payment date	(4) From each interest payment date to maturity	Percent
(1) Redemption value of bond								
Period of time bond is held after issue date (years and months)					Percent	Percent	Percent	Percent
0-6 to 1-0.....	193.75	987.50	4937.50	9875.00	4.00	4.00	6.68	
1-0 to 1-6.....	189.94	979.88	4899.40	9798.80	4.51	5.04	6.80	
1-6 to 2-0.....	486.10	972.20	4861.00	9722.00	4.69	5.07	6.94	
2-0 to 2-6.....	481.87	963.74	4818.70	9637.40	4.75	4.95	7.10	
2-6 to 3-0.....	478.35	956.70	4783.50	9567.00	4.85	5.23	7.26	
3-0 to 3-6.....	475.11	950.22	4751.10	9502.20	4.94	5.44	7.42	
3-6 to 4-0.....	472.07	944.14	4720.70	9441.40	4.02	5.56	7.61	
4-0 to 4-6.....	474.08	948.16	4740.80	9481.60	5.32	7.74	7.59	
4-6 to 5-0.....	482.29	964.58	4822.90	9645.80	5.80	10.32	7.29	
5-0 to 5-6.....	500.00	1000.00	5000.00	10000.00	6.50	14.08	6.50	
5-6 to 6-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
6-0 to 6-6.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
6-6 to 7-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
7-0 to 7-6.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
7-6 to 8-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
8-0 to 8-6.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
8-6 to 9-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
9-0 to 9-6.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
9-6 to 10-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	6.50	
10-0.....	500.00	1000.00	5000.00	10000.00	6.50	6.50	—	

\*The yield from issue to maturity is 6.5 percent.

**Exhibit 6.—Department Circular No. 4-67, First Revision, regulations governing agencies for issue of United States savings bonds**

DEPARTMENT OF THE TREASURY,  
*Washington, December 11, 1979.*

**SUMMARY:** Department of the Treasury Circular, Public Debt Series No. 4-67 (31 CFR, Part 317), contains the regulations governing agencies authorized to sell and issue accrual-type United States Savings Bonds and Notes. The Circular has previously referred specifically to United States Savings Bonds of Series E and to United States Savings Notes (Freedom Shares). This First Revision of the Circular is necessary because of the introduction in 1980 of Series EE savings bonds and the withdrawal from sale of Series E savings bonds. The sale of savings notes terminated on June 30, 1970.

**EFFECTIVE DATE:** January 1, 1980.

**SUPPLEMENTARY INFORMATION:** The Secretary of the Treasury has announced that United States Savings Bonds of Series EE will be offered for sale as of January 1, 1980. Under the terms of the offering circular, the bonds will be sold and issued by organizations qualified as issuing agents. The Secretary has also announced that Series E savings bonds will be withdrawn from sale. Their over-the-counter sales will be terminated as of December 31, 1979, and sales on payroll deduction plans will be terminated no later than June 30, 1980.

In view of the changes in the Savings Bond Program, Department of the Treasury Circular, Public Debt Series No. 4-67, the regulations governing issuing agents, is being revised, effective January 1, 1980, to cover the issuance of Series EE bonds. The revised regulations also apply to Series E bonds until their sale and issue have been terminated and a final accounting has been made by each issuing agent for the Series E savings bond stock for which it is charged.

Other changes being made in the regulations are discussed below.

Some rearrangement and renumbering of the various sections in the circular have been made.

Section 317.3 is being revised to allow qualification of agents only on the basis of trust agreements. Under the regulations previously in effect, there have been three bases for qualification: trust agreement, prepayment agreement and collateral agreement. Since virtually all agents have qualified under trust agreements, the prepayment and collateral agencies are being eliminated. Agents which had qualified under these two latter classifications must requalify under trust agreements.

Section 317.4 provides that organizations currently qualified under trust agreements to issue Series E bonds may sell and issue Series EE bonds without the need for requalification. Issuing agents have been individually notified that their qualification will automatically be extended, but that they may requalify if they so desire.

A new provision of the circular, i.e., Section 317.8, stresses the importance the Department attaches to compliance with its instructions for the prompt remittance of the proceeds of savings bonds sales. These sales proceeds are funds belonging to the United States which are held in trust by issuing agents until properly remitted. The Department recently revised its rules to accelerate the remittance of these proceeds, in line with the President's objective of improving cash management operations within the Federal Government.

Section 317.9, which deals with the role of the Federal Reserve Banks, as fiscal agents, has been expanded.

The regulations in this Part involve the fiscal policy of the United States and do not meet the Department's criteria for significant regulations. Accordingly, it has been determined that notice and public procedures are unnecessary.

The regulations in Title 31, Code of Federal Regulations, Part 317, are revised as follows:

## PART 317—REGULATIONS GOVERNING AGENCIES FOR ISSUE OF UNITED STATES SAVINGS BONDS

### § 317.0 Purpose and effective date.

The regulations in this Part govern the manner in which organizations may qualify and act as agents for the sale and issue of accrual-type United States Savings Bonds. They are effective as of January 1, 1980.

### § 317.1 Definitions.

(a) "Bond(s)" means United States Savings Bonds of Series EE, and , until their sale is terminated, savings bonds of Series E.

(b) "Federal Reserve Bank" refers to the Federal Reserve Bank of the district in which the issuing agent or the applicant organization is located, and includes the Branch(es) of the Reserve Bank, where appropriate.

(c) "Issuing agent" refers to an organization which has been granted a certificate of qualification by a Federal Reserve Bank to sell and issue savings bonds.

(d) "Offering circular" refers to Department of the Treasury Circular, Public Debt Series No. 1-80, and, until the sale of Series E bonds is terminated, Department of the Treasury Circular No. 653.

(e) "Organization" means any entity, as described in § 317.2, which may qualify as an issuing agent of bonds.

### § 317.2 Organizations authorized to act.

Organizations eligible to apply for qualification and serve as savings bond issuing agents include: (a) Banks, trust companies and savings institutions chartered by or incorporated under the laws of the United States, or those of any State or Territory of the United States, the District of Columbia, or the Commonwealth of Puerto Rico; (b) Agencies of the United States and of State and local governments; and (c) Employers operating payroll savings plans for the purchase of United States Savings Bonds.

### § 317.3 Procedure for qualifying and serving as issuing agent.

(a) *Execution of application-agreement.* The applicant-organization shall obtain from, duly execute, and file with the Federal Reserve Bank an application-agreement form. The terms of each application-agreement shall include the provisions prescribed by Section 202 of Executive Order No. 11246, entitled "Equal Employment Opportunity" (3 CFR, Subchapter B, 42 U.S.C. 2000e note).

(b) *Certificate of qualification.* Upon approval of an application-agreement, the Federal Reserve Bank will issue a certificate of qualification to the organization. Until the receipt of such a certificate, an organization shall not perform any act as an issuing agent, or advertise in any manner that it is authorized to so act or that it has applied for qualification as an issuing agent.

(c) *Basis for obtaining stock and performing issue functions.* After receipt of a certificate of qualification, an organization may obtain bond stock and perform the functions of an issuing agent. Under the terms of the application-agreement, the stock of bonds, together with the proceeds of their sale, are at all times the property of the United States, for which the organization shall be fully accountable.

(d) *Adverse action or change in qualification.* An organization will be notified by the Federal Reserve Bank if its application-agreement to act as issuing agent is not approved, or if, after qualification, the certificate of qualification is terminated.

### § 317.4 Issuing agents currently qualified.

Organizations qualified as issuing agents under trust agreements currently in effect are authorized to continue to act in that capacity without requalification. By so acting, they shall be subject to the terms and conditions of the previously executed application-agreements and these regulations in the same manner and to the same extent as though they had requalified hereunder.



### § 317.5 Termination of qualification.

(a) *By the United States.* The Secretary of the Treasury or his delegate may terminate the qualification of an issuing agent at any time, upon due notice to the agent. If this action is taken, the agent will be required to make a final accounting for the balance of savings bond stock for which it is charged, based on the records of the Federal Reserve Bank. The agent must surrender all unissued bonds and remit the issue price of any remaining bonds included in its accountability.

(b) *At request of issuing agent.* A Federal Reserve Bank will terminate the qualification of an issuing agent upon its request, provided the agent is in full compliance with the terms of its agreement and the applicable regulations and instructions, and renders a final accounting.

### § 317.6 Issuance of bonds.

(a) *General.* Issuing agents shall comply with all regulations and instructions issued by the Department of the Treasury directly, or through the Federal Reserve Bank, concerning the sale, inscription, dating, validation and issue of the bonds, and disposition of the registration stubs. No issuing agent shall have authority to sell bonds other than as provided in the offering circular.

(b) *Fees.* Issuing agents other than Federal agencies, which for the purpose of this section include Government corporations and independent establishments, will be paid a fee for each savings bond issued. A schedule reflecting the amount of the fees and the basis upon which they are computed will be published in the Federal Register.

(c) *No charge to customers.* Financial institutions accepting fees from the Treasury for issuing savings bonds shall not make any charge to customers for the same service.

### § 317.7 Accounting for bond stock and sales proceeds.

Issuing agents must comply with all regulations and instructions issued by the Department of the Treasury governing the accounting for bond stock and for the proceeds of bond sales.

### § 317.8 Remittance of sales proceeds.

Issuing agents shall remit bond sales proceeds promptly in accordance with instructions issued by the Department of the Treasury, either directly or through the Federal Reserve Banks. Failure to comply with these instructions may subject an agent to penalties, including termination of its qualification as an issuing agent.

### § 317.9 Role of Federal Reserve Banks.

In their capacity as fiscal agents of the United States, the Federal Reserve Banks are authorized to perform such duties, including the issuance of instructions and forms, as may be necessary to fulfill the purposes and requirements of these regulations. The Reserve Banks qualify issuing agents; supply them with bond stock and maintain records of the agents' accountability; instruct them regarding the sale and issue of bonds, the custody and control of bond stock, and the accounting for and remittance of sales proceeds; and provide guidelines covering the amount of bond stock agents may ordinarily requisition and maintain.

**§ 317.10 Reservation.**

The Secretary of the Treasury may at any time, or from time to time, supplement or amend the terms of these regulations.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 7.—Department Circular No. 3-80, Regulations governing United States savings bonds, Series EE and HH**

DEPARTMENT OF THE TREASURY  
*Washington, December 14, 1979.*

**SUMMARY:** The Department of the Treasury issues final regulations governing United States Savings Bonds of Series EE and HH which are to be placed on sale January 2, 1980. The Department has determined that, for the sake of clarity, some minor modifications should be made in several provisions of the regulations as previously published for comment. The regulations which are now published as a final rule incorporate the clarifying changes which are explained below.

**EFFECTIVE DATE:** January 1, 1980.

**SUPPLEMENTARY INFORMATION:** The Secretary of the Treasury announced earlier this year that the sale of savings bonds of Series E and H would be terminated. Beginning in January 1980, two new series of bonds, Series EE and HH, will be offered.

On June 28, 1979, the Department of the Treasury published in proposed form, the regulations that would govern the United States Savings Bonds of Series EE and HH. The public was invited to submit written comments on these regulations: the period for receiving comments ended on August 15, 1979. Only one response was received. It proposed that each year individuals be allowed to purchase up to \$2,000 (issue price) of Series EE bonds which would be exempt from the Federal income tax if held until the purchaser's retirement. This proposal would require Congressional action since it would involve an amendment of the Internal Revenue Code. Accordingly, it is beyond the scope of these regulations. The suggestion has been forwarded to the Treasury office responsible for tax policy.

The terms and conditions of the Series EE and HH bonds, such as their denominations, maturities, and investment yields, are found in the circulars offering the bonds for sale, i.e., Department of the Treasury Circulars, Public Debt Series Nos. 1-80 and 2-80 (31 CFR, Parts 351 and 352), respectively. Department of the Treasury Circular, Public Debt Series No. 3-80, published below as Part 353 of Title 31, Code of Federal Regulations, contains the regulations governing the two new series of bonds.

All previous series of savings bonds continue to be subject to the regulations in Department of the Treasury Circular No. 530, as revised (31 CFR, Part 315). The differences between the two sets of regulations are briefly discussed below, and minor changes that have been adopted in this final rule are explained.

**Registration and Issue**

In addition to the forms of registration previously authorized for savings bonds by Circular No. 530, Series EE and HH bonds may be inscribed in the name of either parent as natural guardian of a minor. This form of registration allows someone who wants to buy savings bonds for a minor, to name one parent of the child as natural guardian and, hence, the person having responsibility for the bonds.

A specific prohibition on the issuance of bonds in the furtherance of chain letter schemes has been added to the regulations. This provision reflects Treasury policy as to the propriety of purchasing savings bonds for use in chain letter and similar schemes.

### **Limitations on Purchases**

The general limit on purchases of Series EE and HH bonds is \$30,000 and \$20,000 (face amount), respectively, for each calendar year. The current annual limit on Series E and H bonds is \$10,000 (face amount) each. The following special annual limitations are established: \$4,000 (face amount) of Series EE bonds for eligible employee thrift, savings, vacation and similar plans, and \$200,000 (face amount) of Series HH bonds for gifts to tax-exempt organizations.

In the notice of proposed rulemaking published on June 28, 1979, the limitations for Series EE and HH bonds were stated in terms of the "issue price" of the bonds. In Circular No. 530, the limitations are stated in terms of "face amount." For clarity, the final regulations for Series EE and HH bonds use "face amount" as the measure for the limitations on purchases.

### **Relief for Loss or Theft, et cetera**

Time limits have been established for servicing claims for relief that are not filed for a reasonable period after bonds have been redeemed or after the bonds have reached final maturity. If a claim is filed ten or more years after the recorded date of redemption, a copy of the paid bond will not be available for examination by the claimant. A claim filed six or more years after the final maturity of a bond will be processed only if the bond serial number is provided. These limitations will enable the Treasury to realize substantial administrative savings in the costs of maintaining records and servicing claims.

### **Payment**

Under the terms of its offering, a Series EE bond will not be eligible for payment for a period of six months from its issue date. Otherwise, the regulations governing the payment of savings bonds are not essentially changed.

Most banks, trust companies, savings and loan associations, savings banks and other financial institutions are qualified to act as paying agents for Series E or EE bonds. Agents are authorized to pay eligible bonds only to individuals named as owners or coowners. Cases involving payment to surviving beneficiaries or to fiduciaries, organizations, etc., may be processed only by a Federal Reserve Bank or Branch, or the Bureau of the Public Debt, as these transactions often require submission of supporting evidence. If the owner is deceased or disabled, and there is no other person named on the bond who can request payment, instructions should be obtained from a Federal Reserve Bank or Branch or the Bureau of the Public Debt.

Series H and HH bonds are redeemable only at a Federal Reserve Bank or Branch or the Bureau of the Public Debt.

### **Powers of Attorney**

The new savings bond regulations permit limited recognition of powers of attorney to cash bonds where the grantor has specifically authorized the attorney-in-fact to sell or redeem Treasury securities and the power of attorney containing such authority has been executed before a certifying officer. The more common power of attorney will be recognized only in those cases where the grantor has become mentally incompetent or physically disabled, provided the power specifically provides for this contingency. These two provisions operate independently of one another.

### **Reissue**

The new regulations governing reissue differ from those in Circular No. 530 in that the name of a beneficiary may be removed from a Series EE or HH bond upon the registered owner's request alone. The consent of the beneficiary is not required.

In the notice of proposed rulemaking governing reissues of Series EE and HH bonds, no provision was made covering the adoptive relationship. This has been remedied by qualifying the word 'blood', as used in the regulations, to include legal adoption. In addition, the provisions for reissue of bonds registered in coownership form have been rewritten for clarity.



### **Certifying Officer**

Circular No. 530 has not required that requests for reissue or for other types of transactions of savings bonds be signed before an authorized certifying officer as are requests for payment of the bonds. This requirement appears only in the instructions on the reissue applications. To remove any doubt as to whether requests on Public Debt forms must be executed before a certifying officer, a new provision has been added stating that transaction forms must be properly certified, whenever required in the instructions on the form.

### **Deceased Owners**

The Bureau of the Public Debt has pioneered procedures for the disposition of savings bonds belonging to the estates of deceased owners without requiring probate court proceedings. These procedures are being expanded to provide for payment of Series EE and HH bonds to the surviving relatives of a decedent pursuant to a table of precedence.

The minor changes that have been made in the text of the regulations that were published for comment on June 28, 1979, do not affect substantive rights of bondowners. Accordingly, the Fiscal Service is issuing, with the changes described above, Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR, Part 353) as a final rule, effective as of January 1, 1980.

Accordingly, a new Part 353 is added to Title 31 CFR to read as follows:

## **PART 353—REGULATIONS GOVERNING UNITED STATES SAVINGS BONDS, SERIES EE AND HH**

### **SUBPART A—GENERAL INFORMATION**

#### **§ 353.0 Applicability.**

The regulations in this circular, Department of the Treasury Circular, Public Debt Series No. 3-80, govern United States Savings Bonds of Series EE and Series HH. These bonds bear issue dates of January 1, 1980, or thereafter. The regulations in Department of the Treasury Circular No. 530, current revision (31 CFR Part 315), govern all other United States Savings Bonds and Savings Notes.

#### **§ 353.1 Official agencies.**

(a) The Bureau of the Public Debt of the Department of the Treasury is responsible for administering the Savings Bonds Program. Authority to process transactions has been delegated to Federal Reserve Banks and Branches, as fiscal agents of the United States.

(b) Communications concerning transactions and requests for forms should be addressed to (1) a Federal Reserve Bank or Branch; (2) the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101; or (3) the Bureau of the Public Debt, Washington, D.C. 20226. The names and addresses of the Federal Reserve Banks and Branches are:

Federal Reserve Bank of Boston, Boston, Massachusetts 02106.

Federal Reserve Bank of New York, Federal Reserve Post Office Station, New York, New York 10045. Buffalo Branch, Federal Reserve Bank, Box 961, Buffalo, New York 14240.

Federal Reserve Bank of Philadelphia, Box 66, Philadelphia, Pennsylvania 19105.

Federal Reserve Bank of Cleveland, Box 6387, Cleveland, Ohio 44101. Cincinnati Branch, Federal Reserve Bank, Box 999, Cincinnati, Ohio 45201. Pittsburgh Branch, Federal Reserve Bank, Box 867, Pittsburgh, Pennsylvania 15230.

Federal Reserve Bank of Richmond, Box 27622, Richmond, Virginia 23261. Baltimore Branch, Federal Reserve Bank, Box 1378, Baltimore, Maryland 21203. Charlotte Branch, Federal Reserve Bank, Box 300, Charlotte, North Carolina 28230.

Federal Reserve Bank of Atlanta, Atlanta, Georgia, 30303. Birmingham Branch, Federal Reserve Bank, Box 10447, Birmingham, Alabama 35202. Jacksonville Branch, Federal Reserve Bank, Jacksonville, Florida 32203. Miami Branch, Federal Reserve Bank, Box 520847, Miami, Florida 33152. Nashville Branch, Federal Reserve Bank, Nashville, Tennessee 37203. New Orleans Branch, Federal Reserve Bank, Box 61630, New Orleans, Louisiana 70161.

Federal Reserve Bank of Chicago, Box 834, Chicago, Illinois 60690. Detroit Branch, Federal Reserve Bank, Box 1059, Detroit, Michigan 48231.

Federal Reserve Bank of St. Louis, Box 442, St. Louis, Missouri 63166. Little Rock Branch, Federal Reserve Bank, Box 1261, Little Rock, Arkansas 72203. Louisville Branch, Federal Reserve Bank, Box 32710, Louisville, Kentucky 40232. Memphis Branch, Federal Reserve Bank, Box 407, Memphis, Tennessee 38101.

Federal Reserve Bank of Minneapolis, Minneapolis, Minnesota 55480. Helena Branch, Federal Reserve Bank, Helena, Montana 59601.

Federal Reserve Bank of Kansas City, Federal Reserve Station, Kansas City, Missouri 64198. Denver Branch, Federal Reserve Bank, Box 5228, Terminal Annex, Denver, Colorado 80217. Oklahoma City Branch, Federal Reserve Bank, Box 25129, Oklahoma City, Oklahoma 73125. Omaha Branch, Federal Reserve Bank, Omaha, Nebraska 68102.

Federal Reserve Bank of Dallas, Station K, Dallas, Texas 75222. El Paso Branch, Federal Reserve Bank, Box 100, El Paso, Texas 79999. Houston Branch, Federal Reserve Bank, Box 2579, Houston, Texas 77001. San Antonio Branch, Federal Reserve Bank, Box 1471, San Antonio, Texas 78295.

Federal Reserve Bank of San Francisco, Box 7702, San Francisco, California 94120. Los Angeles Branch, Federal Reserve Bank, Box 2077, Terminal Annex, Los Angeles, California 90051. Portland Branch, Federal Reserve Bank, Box 3436, Portland, Oregon 97208. Salt Lake City Branch, Federal Reserve Bank, Box 30780, Salt Lake City, Utah 84125. Seattle Branch, Federal Reserve Bank, Box 3567, Seattle, Washington 98124.

(c) Notices and documents must be filed with the agencies referred to above and as indicated in these regulations.

### § 353.2 Definitions.

(a) “Bond” means a United States Savings Bond of Series EE or HH, unless the context indicates otherwise.

(b) “Incompetent” means an individual who is incapable of handling his or her business affairs because of a legal, mental or medical disability, except that a minor is not an incompetent solely because of age.

(c) “Issuing agent” means an organization that has been qualified under the provisions of Department of the Treasury Circular, Public Debt Series No. 4-67, current revision (31 CFR Part 317), to issue savings bonds.

(d) “Paying agent” means a financial institution that has been qualified under the provisions of Department of the Treasury Circular No. 750, current revision (31 CFR Part 321), to make payment of savings bonds.

(e) “Payment” means redemption, unless otherwise indicated by context.

(f) “Person” means any legal entity including, but without limitation, an individual, corporation (public or private), partnership, unincorporated association, or fiduciary estate.

(g) “Personal trust estates” means trust estates established by natural persons in their own right for the benefit of themselves or other natural persons in whole or in part, and common trust funds comprised in whole or in part of such trust estates.

(h) “Reissue” means the cancellation and retirement of a bond and the issuance of a new bond or bonds of the same series, same issue date, and same total face amount.

(i) “Representative of the estate of a minor, incompetent, aged person, absentee, et al.” means the court-appointed or otherwise qualified person, regardless of title, who is legally authorized to act for the individual. The term does not include parents in their own right, voluntary or natural guardians, or the executors or administrators of decedents’ estates.

(j) “Surrender” means the actual receipt of a bond with an appropriate request for payment or reissue by either a Federal Reserve Bank or Branch, the Bureau of the Public Debt, or, if a paying agent is authorized to handle the transaction, the actual receipt of the bond and the request for payment by the paying agent.

(k) “Taxpayer identifying number” means a social security account number or an employer identification number.

(l) “Voluntary guardian” means an individual who is recognized as authorized to act for an incompetent, as provided by § 353.64.

## SUBPART B-REGISTRATION

## § 353.5 General rules.

(a) *Registration is conclusive of ownership.* Savings bonds are issued only in registered form. The registration must express the actual ownership of, and interest in, the bond. The registration is conclusive of ownership, except as provided in Sec. 353.49.

(b) *Requests for registration.* Registrations requested must be clear, accurate and complete, conform substantially with one of the forms set forth in this Subpart, and include the taxpayer identifying number of the owner or first-named coowner. The taxpayer identifying number of the second-named coowner or beneficiary is not required but its inclusion is desirable. The registration of all bonds owned by the same person, organization, or fiduciary should be uniform with respect to the name of the owner and any description of the fiduciary capacity. An individual should be designated by the name he or she is ordinarily known by or uses in business, including at least one full given name. The name may be preceded or followed by any applicable title, such as "Miss", "Mr.", "Mrs.", "Ms.", "Dr.", "Rev.", "M.D.", or "D.D.". A suffix, such as "Sr." or "Jr.", must be included when ordinarily used or when necessary to distinguish the owner from another member of his family. A married woman's own given name, not that of her husband, must be used; for example, "Mary A. Jones" or "Mrs. Mary A. Jones", NOT "Mrs. Frank B. Jones". The address must include, where appropriate, the number and street, route, or any other local feature, city, State, and ZIP Code.

(c) *Inscription of bonds purchased as gifts.* If the bonds are purchased as gifts, awards, prizes, etc., and the taxpayer identifying number of the intended owner is not known, the purchaser's number must be furnished. In this event, the issuing agent will inscribe the word "GIFT" and the purchaser's number on the bond. Bonds so inscribed will not be associated with the purchaser's own holdings. The registration of a bond in the name of a purchaser with another as coowner or in the purchaser's name with another as beneficiary is not considered a gift or an award.

## § 353.6 Restrictions on registration.

(a) *Natural persons.* Only an individual in his or her own right may be designated as coowner or beneficiary along with any other individual, whether on original issue or reissue, except as provided in § 353.7(f).

(b) *Residence.* The designation of an owner or first-named coowner is restricted, on original issue only, to persons (whether individuals or others) who are:

(1) Residents of the United States, its territories or possessions, or the Commonwealth of Puerto Rico;

(2) Citizens of the United States residing abroad;

(3) Civilian employees of the United States or members of its armed forces, regardless of their residence or citizenship; and

(4) Residents of Canada or Mexico who work in the United States but only if the bonds are purchased on a payroll deduction plan and the owner provides a taxpayer identifying number.

A nonresident alien may be designated coowner or beneficiary or, on authorized reissue, owner, unless the nonresident alien is a resident of an area with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States or its agencies or instrumentalities. See Department of the Treasury Circular No. 655, current revision (31 CFR Part 211). Registration is not permitted in any form which includes the name of any alien who is a resident of any restricted area.

(c) *Minors.* (1) Minors may purchase with their wages, earnings, or other funds belonging to them and under their control bonds registered in their names alone or with a coowner or beneficiary.

(2) Bonds purchased by another person with funds belonging to a minor not under legal guardianship or similar fiduciary estate must be registered, without a coowner or beneficiary, in the name of the minor or a natural guardian on behalf of a minor.



(3) Bonds purchased with funds of another may be registered to name the minor as owner, coowner, or beneficiary. If the minor is under legal guardianship or similar fiduciary estate, the registration must include an appropriate reference to it.

(4) Bonds purchased as a gift to a minor under a gift-to-minors statute must be registered as prescribed by the statute and no coowner or beneficiary may be named.

(5) Bonds purchased by a representative of a minor's estate must be registered in the name of the minor and must include in the registration an appropriate reference to the guardianship or similar fiduciary estate. Bonds purchased by a representative of the estates of two or more minors, even though appointed in a single proceeding, must be registered in the name of each minor separately with appropriate reference to the guardianship or similar fiduciary estate.

(d) *Incompetents.* Bonds may be registered to name as owner, coowner, or beneficiary an incompetent for whose estate a guardian or similar representative has been appointed, except that a coowner or beneficiary may not be named on bonds purchased with funds belonging to the incompetent. The registration must include appropriate reference to the guardianship or similar fiduciary estate. Bonds should not be registered in the name of an incompetent unless there is a representative for his or her estate, except as provided in § 353.64.

### § 353.7 Authorized forms of registration.

Subject to any limitations or restrictions contained in these regulations on the right of any person to be named as owner, coowner, or beneficiary, bonds should be registered as indicated below. A savings bond inscribed in the form not substantially in agreement with one of the forms authorized by this Subpart is not considered validly issued.

(a) *Natural persons.* A bond may be registered in the names of individuals in their own right, but only in one of the forms authorized by this paragraph.

(1) *Single ownership form.* A bond may be registered in the name of one individual. Example: John A. Jones 123-45-6789.

(2) *Coownership form.* A bond may be registered in the names of two individuals in the alternative as coowners. The form of registration "A and B" is not authorized. Examples:

John A. Jones 123-45-6789 or Ella S. Jones 987-65-4321.

John A. Jones 123-45-6789 or (Miss, Ms. or Mrs.) Ella S. Jones.

Ella S. Jones 987-65-4321 or John A. Jones.

(3) *Beneficiary form.* A bond may be registered in the name of one individual payable on death to another. "Payable on death to" may be abbreviated to "P.O.D." Examples:

John A. Jones 123-45-6789 payable on death to Mrs. Ella S. Jones.

John A. Jones 123-45-6789 P.O.D. Ella S. Jones 987-654-4321.

(b) *Fiduciaries (including legal guardians and similar representatives, certain custodians, natural guardians, executors, administrators, and trustees).*

(1) *General.* A bond may be registered in the name of any person or persons or any organization acting as fiduciary of a single fiduciary estate, but not where the fiduciary will hold the bond merely or principally as security for the performance of a duty, obligation, or service. Registration should conform to a form authorized by this paragraph. A coowner or beneficiary may be named only in accordance with the applicable provisions of § 353.6(c) and (d). A common trust fund established and maintained by a financial institution authorized to act as a fiduciary will be considered a single fiduciary estate within the meaning of these regulations.

(2) *Legal guardians, conservators, similar representatives, certain custodians.* A bond may be registered in the name and title or capacity of the legally appointed or authorized representative of the estate of a minor, incompetent, aged or infirm person, absentee, et al., or in the name of that individual followed by an appropriate reference to the estate. Examples:

Tenth National Bank, guardian (or conservator, trustee, etc.) of the estate of George N. Brown 123-45-6789, a minor (or an incompetent, aged person, infirm person, or absentee).

Henry C. Smith, conservator of the estate of John R. White 123-45-6789, an adult, pursuant to Sec. 633.572 of the Iowa Code.

John F. Green 123-45-6789, a minor (or an incompetent) under custodianship by designation of the Veterans Administration.

Frank M. Redd 123-45-6789, an incompetent for whom Eric A. Redd has been designated trustee by the Department of the Army pursuant to 37 U.S.C. 602.

Arnold A. Ames, as custodian for Barry B. Bryan 123-45-6789, under the California Uniform Gifts to Minors Act.

Thomas J. Reed, as custodian for Lawrence W. Reed 123-45-6789, a minor, under the laws of Georgia.

Richard A. Rowe 123-45-6789, for whom Reba L. Rowe is representative payee for social security benefits (or black lung benefits, as the case may be). (If the beneficiary is a minor, the words "a minor" should appear immediately after the social security number.)

Henry L. Green 123-45-6789 or George M. Brown, a minor under legal guardianship of the Tenth National Bank.

Henry L. Green 123-45-6789 P.O.D. George M. Brown, a minor under legal guardianship of the Tenth National Bank.

Redd State Hospital and School, selected payee for John A. Jones 123-45-6789, a Civil Service annuitant, pursuant to 5 U.S.C. 8345(e).

(3) *Natural guardians.* A bond may be registered in the name of either parent (natural and adoptive) of a minor, as natural guardian. The registration of a bond in this form is considered as establishing a fiduciary relationship. A coowner or beneficiary may be named but only if the funds used to purchase the bonds do not belong to the minor. Examples:

John A. Jones, as natural guardian for Henry M. Jones 123-45-6789.

Melba Smith, as natural guardian for Thelma Smith 123-45-6789 P.O.D. Bartholomew Smith.

(4) *Executors and administrators.* A bond may be registered in the name of the representative appointed by a court to act for an estate of a decedent, or in the name of an executor authorized to administer a trust under the terms of a will although not named trustee. The name and capacity of all the representatives as shown in the letters of appointment must be included in the registration and be followed by an adequate identifying reference to the estate. Examples:

John H. Smith and Calvin N. Jones, executors of the will (or administrators of the estate) of Robert J. Smith, deceased, 12-3456789.

John H. Smith, executor of the will of Robert J. Smith, deceased, in trust for Mrs. Jane L. Smith, with remainder over, 12-3456789.

(5) *Trustees or life tenants under wills, deeds of trust, agreements, or similar instruments.* A bond may be registered in the name and title of the trustee of a trust estate, or in the name of a life tenant, followed by an adequate identifying reference to the authority governing the trust or life tenancy. Examples:

Thomas J. White and Tenth National Bank, trustees under the will of Robert J. Smith, deceased, 12-3456789.

Jane N. Black 123-45-6789, life tenant under the will of Robert J. Black, deceased.

Tenth National Bank, trustee under agreement with Paul E. White, dated 2/1/80, 12-3456789.

Carl A. Black and Henry B. Green, trustees under agreement with Paul E. White, dated 2/1/80, 12-3456789.

Paul E. White, trustee under declaration of trust dated 2/1/80, 12-3456789.

(i) If the trust instrument designates by title only an officer of a board or an organization as trustee, only the title of the officer should be used. Example:

Chairman, Board of Trustees, First Church of Christ, Scientist, of Chicago, Illinois, in trust under the will of Robert J. Smith, deceased, 12-3456789.

(ii) The names of all trustees, in the form used in the trust instrument, must be included in the registration, except as follows:

(A) If there are several trustees designated as a board or they are required to act as a unit, their names may be omitted and the words "Board of Trustees" substituted for the word 'trustee'. Example:

Board of Trustees of Immediate Relief Trust of Federal Aid Association, under trust indenture dated 2/1/80, 12-3456789.

(B) If the trustees do not constitute a board or are not required to act as a unit, and are too numerous to be designated in the registration by names and title, some or all the names may be omitted. Examples:

John A. Smith, Henry B. Jones, et al., trustees under the will of Edwin O. Mann, deceased, 12-3456789.

Trustees under the will of Edwin O. Mann, deceased, 12-3456789.

(6) *Employee thrift, savings, vacation and similar plans.* A bond may be registered in the name and title, or title alone, of the trustee of an eligible employee thrift, savings, vacation or similar plan, as defined in § 353.13(a). If the instrument creating the trust provides that the trustees shall serve for a limited term, their names may be omitted. Examples:

Tenth National Bank, trustee of Pension Fund of Safety Manufacturing Company, U/A with the company, dated March 31, 1980, 12-3456789.

Trustees of Retirement Fund of Safety Manufacturing Company, under directors' resolution adopted March 31, 1980, 12-3456789.

County Trust company, trustee of the Employee Savings Plan of Jones Company, Inc., U/A dated January 17, 1980, 12-3456789.

Trustee of the Employee Savings Plan of Brown Brothers, Inc., U/A dated January 20, 1980, 12-3456789.

(7) *Funds of lodges, churches, societies, or similar organizations.* A bond may be registered in the title of the trustees, or a board of trustees, holding funds in trust for a lodge, church, or society, or similar organization, whether or not incorporated. Examples:

Trustees of the First Baptist Church, Akron, Ohio, acting as a Board under Section 15 of its bylaws, 12-3456789.

Trustees of Jamestown Lodge No. 1000, Benevolent and Protective Order of Elks, under Section 10 of its bylaws, 12-3456789.

Board of Trustees of Lotus Club, Washington, Indiana, under Article 10 of its constitution, 12-3456789.

(8) *Investment agents for religious, educational, charitable and non-profit organizations.* A bond may be registered in the name of a bank, trust company, or other financial institution, or an individual, as agent under an agreement with a religious, educational, charitable or non-profit organization, whether or not incorporated, if the agent holds funds for the sole purpose of investing them and paying the income to the organization. The name and designation of the agent must be followed by an adequate reference to the agreement. Examples:

Tenth National Bank, fiscal agent U/A with the Evangelical Lutheran Church of the Holy Trinity, dated 12/28/80, 12-3456789.

Sixth Trust Company, Investment Agent U/A dated September 16, 1980, with Central City Post, Department of Illinois, American Legion, 12-3456789.

John Jones, Investment Agent U/A dated September 16, 1980, with Central City Post, Department of Illinois, American Legion, 12-3456789.

(9) *Funds of school groups or activities.* A bond may be registered in the title of the principal or other officer of a public, private, or parochial school holding funds in trust for a student body fund or for a class, group, or activity. If the amount purchased for any one fund does not exceed \$2,500 (face amount), no reference need be made to a trust instrument. Examples:

Principal, Western High School, in trust for the Class of 1980 Library Fund, 12-3456789.

Director of Athletics, Western High School, in trust for Student Activities Association, under resolution adopted 5/12/80, 12-3456789.

(10) *Public corporations, bodies, or officers as trustees.* A bond may be registered in the name of a public corporation or a public body, or in the title of a public officer, acting as trustee under express authority of law, followed by an appropriate reference to the statute creating the trust. Examples:

Rhode Island Investment Commission, trustee of the General Sinking Fund under Title 35, Ch. 8, Gen. Laws of Rhode Island.

Superintendent of the Austin State Hospital Annex, in trust for the Benefit Fund under Article 3183C, Vernon's Civ. Stat. of Texas Ann.

(c) *Private organizations (corporations, associations, partnerships).* (1) *General.* A bond may be registered in the name of any private organization in its own right. The full legal name of the organization as set forth in its charter, articles of incorporation,



constitution, partnership agreement, or other authority from which its powers are derived, must be included in the registration and may be followed by a parenthetical reference to a particular account other than a trust account.

(2) *Corporations.* A bond may be registered in the name of a business, fraternal, religious, non-profit, or other private corporation. The words "a corporation" must be included in the registration unless the fact of incorporation is shown in the name. Examples:

Smith Manufacturing Company, a corporation, 12-3456789.  
Green and Redd, Inc., 12-3456789 (Depreciation Acct.)

(3) *Unincorporated associations.* A bond may be registered in the name of a club, lodge, society, or a similar self-governing association which is unincorporated. The words "an unincorporated association" must be included in the registration. This form of registration must not be used for a trust fund, board of trustees, a partnership, or a sole proprietorship. If the association is chartered by or affiliated with a parent organization, the name or designation of the subordinate or local organization must be given first, followed by the name of the parent organization. The name of the parent organization may be placed in parentheses and, if well known, may be abbreviated. Examples:

The Lotus Club, an unincorporated association, 12-3456789.  
Local 447, Brotherhood of Railroad Trainmen, an unincorporated association, 12-3456789.  
Eureka Lodge 317 (A.F. and A.M.), an unincorporated association, 12-3456789.

(4) *Partnerships.* A bond may be registered in the name of a partnership. The words "a partnership" must be included in the registration. Examples:

Smith & Jones, a partnership, 12-3456789.  
Acme Novelty Company, a partnership, 12-3456789.

(5) *Sole Proprietorships.* A bond may be registered in the name of an individual who is doing business as a sole proprietor. A reference may be made to the trade name under which the business is conducted. Example:

John Jones DBA Jones Roofing Company 123-45-6789.

(d) *Institutions (churches, hospitals, homes, schools, etc.).* A bond may be registered in the name of a church, hospital, home, school, or similar institution conducted by a private organization or by private trustees, regardless of the manner in which it is organized or governed or title to its property is held. Descriptive words, such as "a corporation" or "an unincorporated association", must not be included in the registration. Examples:

Shriners' Hospital for Crippled Children, St. Louis, Missouri, 12-3456789.  
St. Mary's Roman Catholic Church, Albany, New York, 12-3456789.  
Rodeph Shalom Sunday School, Philadelphia, Pennsylvania, 12-3456789.

(e) *States, public bodies and corporations, and public officers.* A bond may be registered in the name of a State, county, city, town, village, school district, or other political entity, public body, or corporation established by law (including a board, commission, administration, authority, or agency) which is the owner or official custodian of public funds, other than trust funds, or in the full legal title of the public officer having custody of the funds. Examples:

State of Maine.  
Town of Rye, New York (Street Improvement Fund).  
Maryland State Highway Administration.  
Treasurer, City of Chicago.

(f) *The United States Treasury.* A person who desires to have a bond become the property of the United States upon his or her death may designate the United States Treasury as coowner or beneficiary. Examples:

George T. Jones 123-45-6789 or the United States Treasury.  
George T. Jones 123-45-6789 P.O.D. the United States Treasury.

### § 353.8 Chain letters prohibited.

The issuance of bonds in the furtherance of a chain letter or pyramid scheme is considered to be against the public interest and is prohibited.

## SUBPART C—LIMITATIONS ON ANNUAL PURCHASES

### § 353.10 Amounts which may be purchased.

The amount of savings bonds of Series EE and HH which may be purchased and held, in the name of any one person in any one calendar year, is computed according to the provisions of § 353.11 and is limited as follows:

- (a) *Series EE.* (1) *General annual limitation.* \$30,000 (face amount).
- (2) *Special limitation.* \$4,000 (face amount) multiplied by the highest number of employees participating in an eligible employee plan, as defined in § 353.13, at any time during the calendar year in which the bonds are issued.
- (b) *Series HH.*
  - (1) *General annual limitation.* \$20,000 (face amount).
  - (2) *Special limitation.* \$200,000 (face amount) for bonds received in a calendar year as gifts by an organization which at the time of purchase was an exempt organization under the terms of 26 CFR 1.501(c)(3)-1.

### § 353.11 Computation of amount.

(a) *General.* The purchases of bonds in the name of any person in an individual capacity are computed separately from purchases in a fiduciary capacity. A pension or retirement fund, or an investment, insurance, annuity, or similar fund or trust is regarded as an entity, regardless of the number of beneficiaries or the manner in which their shares or interests are established, determined, or segregated.

(b) *Bonds included in computation.* In computing the purchases for each person, the following outstanding bonds are included:

- (1) All bonds registered in the name of that person alone;
- (2) All bonds registered in the name of the representative of the estate of that person; and
- (3) All bonds registered in the name of that person as coowner. However, in computing the amount of bonds of each series held in coownership form, the limitation may be applied to the holdings of either of the coowners or apportioned between them.

(c) *Bonds excluded from computation.* In computing the purchases for each person, the following are excluded:

- (1) Bonds on which that person is named beneficiary;
- (2) Bonds to which that person has become entitled—
  - (i) Under § 353.70 as surviving beneficiary upon the death of the registered owner;
  - (ii) As an heir or a legatee of the deceased owner;
  - (iii) By virtue of the termination of a trust or the happening of a similar event;
- (3) Bonds issued in an authorized exchange or reinvestment; and
- (4) Bonds that are purchased and redeemed within the same calendar year.

### § 353.12 Disposition of excess.

If any person at any time has savings bonds issued during any one calendar year in excess of the prescribed amount, instructions should be obtained from the Bureau of the Public Debt, Parkersburg, West Virginia 26101, for appropriate adjustment of the excess. Under the conditions specified in § 353.90, the Commissioner of the Public Debt may permit excess purchases to stand in any particular case or class of cases.

### § 353.13 Employee plans—Conditions of eligibility.

(a) *Definition of plan.* Employee thrift, savings, vacation and similar plans are contributory plans established by the employer for the exclusive and irrevocable benefit of its employees or their beneficiaries. Each plan must afford employees the means of making regular savings from their wages through payroll deductions and provide for employer contributions to be added to these savings.

(b) *Definition of terms used in this section.* (1) The term "assets" means all the employees' contributions and assets purchased with them and the employer's contributions and assets purchased with them, as well as accretions, such as dividends on stock, the increment in value on bonds and all other income; but, notwithstanding any other provision of this section, the right to demand and receive "all assets" credited to the account of an employee shall not be construed to require the distribution of assets in kind when it would not be possible or practicable to make such a distribution; for example, Series EE bonds may not be reissued in unauthorized denominations.

(2) The word "beneficiary" means (i) the person or persons, if any, designated by the employee in accordance with the terms of the plan to receive the benefits of the plan upon the employee's death or (ii) the estate of the employee.

(c) *Conditions of eligibility.* An employee plan must conform to the following rules in order to be eligible for the special limitation provided in § 353.10.

(1) *Crediting of assets.* All assets of a plan must be credited to the individual accounts of participating employees and may be distributed only to them or their beneficiaries, except as provided in subparagraph (3).

(2) *Purchase of bonds.* Bonds may be purchased only with assets credited to the accounts of participating employees and only if the amount taken from any account at any time for that purpose is equal to the purchase price of a bond or bonds in an authorized denomination or denominations, and shares in the bonds are credited to the accounts of the individuals from which the purchase price was derived, in amounts corresponding with their shares. For example, if \$50 credited to the account of John Jones is commingled with funds credited to the accounts of other employees to make a total of \$5,000 with which a Series EE bond in the denomination of \$10,000 (face amount) is purchased in December 1980 and registered in the name and title of the trustee, the plan must provide, in effect, that John Jones' account be credited to show that he is the owner of a Series EE bond in the denomination of \$100 (face amount) bearing an issue date of December 1, 1980.

(3) *Irrevocable right of withdrawal.* Each participating employee has an irrevocable right to request and receive from the trustee all assets credited to the employee's account or their value, if he or she prefers, without regard to any condition other than the loss or suspension of the privilege of participating further in the plan. However, a plan may limit or modify the exercise of any such right by providing that the employer's contribution does not vest absolutely until the employee shall have made contributions under the plan in each of not more than 60 calendar months succeeding the month for which the employer's contribution is made.

(4) *Rights of beneficiary.* Upon the death of an employee, his or her beneficiary shall have the absolute and unconditional right to demand and receive from the trustee all assets credited to the account of the employee or their value, if he or she so prefers.

(5) *Reissue or payment upon distribution.* When settlement is made with an employee or his or her beneficiary with respect to any bond registered in the name and title of the plan trustee in which the employee has a share, the bond must be paid or reissued to the extent of the share. If an employee or the beneficiary is to receive distribution in kind, bonds bearing the same issue dates as those credited to the employee's account will be reissued in the name of the employee or the employee's beneficiary to the extent entitled, in authorized denominations, in any authorized form of registration, upon the request and certification of the trustee.

(d) *Application for special limitation.* A trustee of an employee plan who desires to purchase bonds under the special limitation should submit to the Federal Reserve Bank of the district a copy of (i) the plan, (ii) any instructions issued under the plan that concern Series EE bonds, and (iii) the trust agreement, in order to establish the plan's eligibility.

(e) *Vacation plans.* Savings bonds may be purchased under certain vacation plans. Questions concerning the eligibility of these plans to purchase bonds in excess of the general limitation should be addressed to the Bureau of the Public Debt, Parkersburg, West Virginia 26101.



## SUBPART D—LIMITATIONS ON TRANSFER OR PLEDGE

**§ 353.15 Transfer.**

Savings bonds are not transferable and are payable only to the owners named on the bonds, except as specifically provided in these regulations and then only in the manner and to the extent so provided.

**§ 353.16 Pledge**

A savings bond may not be hypothecated, pledged, or used as security for the performance of an obligation.

## SUBPART E—JUDICIAL PROCEEDINGS

**§ 353.20 General**

(a) The Department of the Treasury will not recognize a judicial determination that gives effect to an attempted voluntary transfer inter vivos of a bond, or a judicial determination that impairs the rights of survivorship conferred by these regulations upon a coowner or beneficiary. All provisions of this Subpart are subject to these restrictions.

(b) The Department of the Treasury will recognize a claim against an owner of a savings bond and conflicting claims of ownership of, or interest in, a bond between coowners or between the registered owner and the beneficiary, if established by valid judicial proceedings, but only as specifically provided in this Subpart. Section 353.23 specifies the evidence required to establish the validity of the judicial proceedings.

(c) The Department of the Treasury and the agencies that issue, reissue, or redeem savings bonds will not accept a notice of an adverse claim or notice of pending judicial proceedings, nor undertake to protect the interests of a litigant not in possession of a savings bond.

**§ 353.21 Payment to judgment creditors.**

(a) *Purchaser or officer under levy.* The Department of the Treasury will pay (but not reissue) a savings bond to the purchaser at a sale under a levy or to the officer authorized under appropriate process to levy upon property of the registered owner or coowner to satisfy a money judgment. Payment will be made only to the extent necessary to satisfy the money judgment. The amount paid is limited to the redemption value 60 days after the termination of the judicial proceedings. Payment of a bond registered in coownership form pursuant to a judgment or a levy against only one coowner is limited to the extent of that coowner's interest in the bond. That interest must be established by an agreement between the coowners or by a judgment, decree, or order of a court in a proceeding to which both coowners are parties.

(b) *Trustee in bankruptcy, receiver, or similar court officer.* The Department of the Treasury will pay, at current redemption value, a savings bond to a trustee in bankruptcy, a receiver of an insolvent's estate, a receiver in equity, or a similar court officer under the provisions of paragraph (a) of this section.

**§ 353.22 Payment or reissue pursuant to judgment.**

(a) *Divorce.* The Department of the Treasury will recognize a divorce decree that ratifies or confirms a property settlement agreement disposing of bonds or that otherwise settles the interests of the parties in a bond. Reissue of a savings bond may be made to eliminate the name of one spouse as owner, coowner, or beneficiary or to substitute the name of one spouse for that of the other spouse as owner, coowner, or beneficiary pursuant to the decree. However, if the bond is registered in the name of one spouse with another person as coowner, there must be submitted either (1) a request for reissue by the other person or (2) a certified copy of a judgment, decree, or court order entered in proceedings to which the other person and the spouse named on the bond are parties, determining the extent of the interest of that spouse in the bond. Reissue will be permitted only to the extent of that spouse's interest. The evidence required under § 353.23 must be submitted in every case. When the divorce decree

does not set out the terms of the property settlement agreement, a certified copy of the agreement must be submitted. Payment, rather than reissue, will be made if requested.

(b) *Gift causa mortis*. A savings bond belonging solely to one individual will be paid or reissued at the request of the person found by a court to be entitled by reason of a gift causa mortis from the sole owner.

(c) *Date for determining rights*. When payment or reissue under this section is to be made, the rights of the parties will be those existing under the regulations current at the time of the entry of the final judgment, decree, or court order.

### § 353.23 Evidence.

(a) *General*. To establish the validity of judicial proceedings, certified copies of the final judgment, decree, or court order, and of any necessary supplementary proceedings, must be submitted. If the judgment, decree, or court order was rendered more than six months prior to the presentation of the bond, there must also be submitted a certification from the clerk of the court, under court seal, dated within six months of the presentation of the bond, showing that the judgment, decree, or court order is in full force.

(b) *Trustee in bankruptcy or receiver of an insolvent's estate*. A request for payment by a trustee in bankruptcy or a receiver of an insolvent's estate must be supported by appropriate evidence of appointment and qualification. The evidence must be certified by the clerk of the court, under court seal, as being in full force on a date that is not more than six months prior to the presentation of the bond.

(c) *Receiver in equity or similar court officer*. A request for payment by a receiver in equity or a similar court officer, other than a receiver of an insolvent's estate, must be supported by a copy of an order that authorizes the presentation of the bond for redemption, certified by the clerk of the court, under court seal, as being in full force on a date that is not more than six months prior to the presentation of the bond.

## SUBPART F—RELIEF FOR LOSS, THEFT, DESTRUCTION, MUTILATION, DEFACEMENT, OR NONRECEIPT OF BONDS

### § 353.25 General.

Relief, by the issue of a substitute bond or by payment, is authorized for the loss, theft, destruction, mutilation, or defacement of a bond after receipt by the owner or his or her representative. As a condition for granting relief, the Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may require a bond of indemnity, in the form, and with the surety, or security, he considers necessary to protect the interests of the United States. In all cases the savings bond must be identified by serial number and the applicant must submit satisfactory evidence of the loss, theft, or destruction, or a satisfactory explanation of the mutilation or defacement.

### § 353.26 Application for relief—After receipt of bond.

(a) If the serial numbers of the lost, stolen, or destroyed bonds are known, the claimant should execute an application for relief on the appropriate form and submit it to the Bureau of the Public Debt, Parkersburg, West Virginia 26101.

(b) If the bond serial number is not known, the claimant must provide sufficient information to enable the Bureau of the Public Debt to identify the bond by serial number. See § 353.29(c). The Bureau will furnish the proper application form and instructions.

(c) If applicable, a defaced bond and all available fragments of a mutilated bond should be submitted to the Bureau.

(d) The application must be made by the person or persons (including both coowners, if living) authorized under these regulations to request payment of the bond. In addition:

(1) If the bond is in beneficiary form and the owner and beneficiary are both living, both will ordinarily be required to join in the application.

(2) If a minor named on a bond as owner, coowner, or beneficiary is not of sufficient competency and understanding to request payment, both parents will ordinarily be required to join in the application.

(e) If the application is approved, relief will be granted either by the issuance of a bond bearing the same issue date as the bond for which the claim was filed or by the issuance of a check in payment.

#### **§ 353.27 Application for relief—Nonreceipt of bond.**

If a bond issued on any transaction is not received, the issuing agent must be notified as promptly as possible and given all information available about the nonreceipt. An appropriate form and instructions will be provided. If the application is approved, relief will be granted by the issuance of a bond bearing the same issue date as the bond that was not received.

#### **§ 353.28 Recovery or receipt of bond before or after relief is granted.**

(a) If a bond reported lost, stolen, destroyed, or not received, is recovered or received before relief is granted, the Bureau of the Public Debt, Parkersburg, West Virginia 26101, must be notified promptly.

(b) A bond for which relief has been granted is the property of the United States and, if recovered, must be promptly submitted to the Bureau of the Public Debt, Parkersburg, West Virginia 26101, for cancellation.

#### **§ 353.29 Adjudication of claims.**

(a) *General.* The Bureau of the Public Debt will adjudicate claims for lost, stolen or destroyed bonds on the basis of records created and regularly maintained in the ordinary course of business.

(b) *Claims filed 10 years after payment.* A bond for which no claim has been filed within 10 years of the recorded date of redemption will be presumed to have been properly paid. If a claim is subsequently filed, a photographic copy of the bond will not be available to support the disallowance.

(c) *Claims filed six years after final maturity.* No claim filed six years or more after the final maturity of a savings bond will be entertained unless the claimant supplies the serial number of the bond.

### **SUBPART G—INTEREST**

#### **§ 353.30 Series EE bonds.**

Series EE bonds are issued at a discount. The accrued interest is added to the issue price at stated intervals and is payable only at redemption as part of the redemption value. Information regarding interest rates and redemption values is found in Department of the Treasury Circular, Public Debt Series No. 1-80 (31 CFR Part 351).

#### **§ 353.31 Series HH bonds.**

(a) *General.* Series HH bonds are current-income bonds issued at par (face amount). Interest on a Series HH bond is paid semiannually by check, beginning six months from issue date. Interest ceases at maturity, or, if a bond is redeemed before maturity, as of the end of the preceding interest payment period. For example, if a bond on which interest is payable on January 1 and July 1 is redeemed on September 1, interest ceases as of the preceding July 1, and no adjustment of interest will be made for the period from July 1 to September 1. However, if the date of redemption falls on an interest payment date, interest ceases on that date. Information regarding interest rates is found in Department of the Treasury Circular, Public Debt Series No. 2-80 (31 CFR Part 352).

(b) *Redemption value.* Series HH bonds acquired in an authorized exchange or reinvestment are redeemable at face amount. An interest adjustment will be made upon redemption of Series HH bonds purchased for cash, if redeemed within a limited period of time after issue; if held beyond this period, they are redeemable at face amount. Information as to the amount of the interest adjustment and the time period to



which it applies is found in Department of the Treasury Circular, Public Debt Series No. 2-80 (31 CFR Part 352).

(c) *Payment of interest.* Series HH bond interest accounts are maintained by the Bureau of the Public Debt, Parkersburg, West Virginia 26101. Interest will be paid on each interest payment date by check mailed to the address specified for the delivery of checks in the purchase application, exchange subscription, notification of change of address or request for reissue. If no instruction is given as to the delivery of interest checks, the address inscribed on the bond for the owner or the first-named coowner will be used.

(d) *Delivery of interest.* (1) *Notices affecting delivery of interest checks.* To insure appropriate action, notices affecting the delivery of interest checks on Series HH bonds, including changes of addresses, must be received by the Bureau of the Public Debt, Parkersburg, West Virginia 26101, at least one month prior to the interest payment date. Each notice must identify the bonds by the name and taxpayer identifying number of the bondowner. The notice must be signed by the owner or coowner, or, in the case of a minor or incompetent, as provided in paragraph (e) or (f) of this section.

(2) *Owner or coowner deceased.* (i) *Sole owner.* Upon receipt of notice of the death of the owner of a bond, payment of interest on the bond will be suspended until satisfactory evidence is submitted as to who is authorized to endorse and collect interest checks on behalf of the estate of the decedent, in accordance with the provisions of Subpart L.

(ii) *Coowner.* Upon receipt of notice of the death of the coowner to whom interest is being mailed, payment of interest will be suspended until a request for change of address is received from the other coowner, if living, or, if not, until satisfactory evidence is submitted as to the individual who is authorized to endorse and collect interest checks on behalf of the estate of the last deceased coowner, in accordance with the provisions of Subpart L.

(iii) *Owner with beneficiary.* In the case of a bond registered in the form "A payable on death to B", the check will be drawn to the order of "A" alone unless the Bureau of the Public Debt, Parkersburg, West Virginia 26101, receives notice of A's death. In that event, the payment of interest will be suspended until the bond is presented for payment or reissue. Interest so withheld will be paid to the person entitled to the bond.

(e) *Representative appointed for the estate of a minor, incompetent, absentee, et al.* Interest on Series HH bonds is paid in accordance with the provisions of § 353.60 to the representative appointed for the estate of an owner who is a minor, incompetent, absentee, et al. If the registration of the bonds does not include reference to the owner's status, the bonds should be submitted for reissue to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt, Parkersburg, West Virginia 26101, so that interest checks may be properly drawn and delivered. They must be accompanied by the proof of appointment required by § 353.60.

(f) *Adult incompetent's estate having no representative.* If an adult owner of a Series HH bond is incompetent to endorse and collect the interest checks and no legal guardian or similar representative has been appointed to act for him or her, the relative, or other person, responsible for his or her care and support, may apply to the Bureau of the Public Debt for recognition as voluntary guardian for the purpose of receiving, endorsing, and collecting the checks.

(g) *Reissue during interest period.* Physical reissue of a Series HH bond will be made without regard to interest payment dates. The Series HH interest accounts maintained by the Bureau of the Public Debt will be closed in the first week of the month preceding each interest payment date. Interest checks will be drawn to the order of the persons shown to be entitled on these accounts as of the date the accounts are closed.

(h) *Endorsement of checks.* Interest checks must be endorsed in accordance with the regulations governing the endorsement and payment of Government warrants and checks, which are contained in Department of the Treasury Circular No. 21, current revision (31 CFR Part 240).

(i) *Nonreceipt or loss of check.* If an interest check is not received or is lost after receipt, the Bureau of the Public Debt, Parkersburg, West Virginia 26101, should be notified and advised of the bond serial number, the inscription on the bond, including the taxpayer identifying number of the bondowner, and the interest payment date.

## SUBPART H—GENERAL PROVISIONS FOR PAYMENT

**§ 353.35 Payment (redemption).**

(a) *General.* Payment of a savings bond will be made to the person or persons entitled under the provisions of these regulations, except that checks in payment will not be delivered to addresses in areas with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States. See Department of the Treasury Circular No. 655, current revision (31 CFR Part 211). Payment will be made without regard to any notice of adverse claims to a bond and no stoppage or caveat against payment of a bond will be entered.

(b) *Series EE.* A Series EE bond will be paid at any time after six months from issue date at the current redemption value shown in Department of the Treasury Circular, Public Debt Series No. 1-80 (31 CFR Part 351).

(c) *Series HH.* A Series HH bond will be paid at any time after six months from issue date. A Series HH bond issued in an authorized exchange or reinvestment transaction will be paid at face amount. A Series HH bond issued for cash will be paid at the current redemption value shown in Department of the Treasury Circular, Public Debt Series No. 2-80 (31 CFR Part 352). If the bond is redeemed at less than face value, the difference represents an adjustment of interest. A Series HH bond received during the month preceding an interest payment date will not be paid until that date.

**§ 353.36 Payment during life of sole owner.**

A savings bond registered in single ownership form (i.e., without a coowner or beneficiary) will be paid to the owner during his or her lifetime upon surrender with an appropriate request.

**§ 353.37 Payment during lives of both coowners.**

A savings bond registered in coownership form will be paid to either coowner upon surrender with an appropriate request, and upon payment (as determined in § 353.43), the other coowner will cease to have any interest in the bond. If both coowners request payment, payment will be made by check drawn in the form, "John A. Jones AND Mary C. Jones".

**§ 353.38 Payment during lifetime of owner of beneficiary bond.**

A savings bond registered in beneficiary form will be paid to the registered owner during his or her lifetime upon surrender with an appropriate request. Upon payment (as determined in § 353.43) the beneficiary will cease to have any interest in the bond.

**§ 353.39 Surrender for payment.**

(a) *Procedure for bonds of Series EE, in the names of individual owners or coowners only.* An individual who is the owner or coowner of a Series EE bond may present the bond to an authorized paying agent for redemption. The presenter must be prepared to establish his or her identity in accordance with Treasury instructions and identification guidelines. The owner or coowner must sign the request for payment on the bond or, if authorized, on a separate detached request, and add his or her address. If the request for payment has been signed, or signed and certified, before presentation of the bond, the paying agent must be satisfied that the person presenting the bond for payment is the owner or coowner and may require the person to sign the request for payment again. If the bond is in order for payment, the paying agent will make immediate payment at the current redemption value without charge to the presenter. Paying agents are not authorized to process any case involving partial redemption or any case in which supporting evidence is required.

(b) *Procedure for all other cases.* In the case of bonds to which the procedure in paragraph (a) does not apply, or if otherwise preferred, the owner or coowner, or other person entitled to payment, should appear before an officer authorized to certify requests for payment, establish his or her identity, sign the request for payment, and provide information as to the address to which the check in payment is to be mailed. The bond must be forwarded to a Federal Reserve Bank or Branch or the Bureau of the Public Debt. Usually, payment will be expedited by submission to a Federal

Reserve Bank or Branch. In all cases, the cost and risk of presentation of a bond will be borne by the owner. Payment will be made by check drawn to the order of the registered owner or other person entitled and will be mailed to the address requested.

(c) *Date of request.* Requests executed more than six months before the date of receipt of a bond for payment will not be accepted. Neither will a bond be accepted if payment is requested as of a date more than three months in the future.

#### § 353.40 Special provisions for payment

(a) *Owner's signature not required.* A bond may be paid by a paying agent or Federal Reserve Bank without the owner's signature to the request for payment, if the bond bears the special endorsement of a paying agent specifically qualified to place such an endorsement on savings bonds.

(b) *Signature by mark.* A signature by mark (X) must be witnessed by at least one disinterested person and a certifying officer. See Subpart J. The witness must attest to the signature by mark substantially as follows: "Witness to signature by mark", followed by his or her signature and address.

(c) *Name change.* If the name of the owner, coowner, or other person entitled to payment, as it appears in the registration or in evidence on file in the Bureau of the Public Debt, has been changed in any legal manner, the signature to the request for payment must show both names and the manner in which the change was made; for example, "Mary T. Jones Smith (Mary T. J. Smith or Mary T. Smith) changed by marriage from Mary T. Jones", or "John R. Young, changed by order of court from Hans R. Jung". See § 353.50.

(d) *Attorneys-in-fact.* A request for payment signed by an attorney-in-fact will be recognized if it is accompanied by a copy of a power of attorney, executed before a certifying officer, that authorizes the attorney-in-fact to sell or redeem the grantor's Treasury securities. See § 353.65 for separate rules relating to the use of powers of attorney for incompetent or physically disabled individuals.

#### § 353.41 Partial redemption.

A bond of Series EE or HH may be redeemed in part at current redemption value, but only in amounts corresponding to authorized denominations, upon surrender of the bond to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt in accordance with § 353.39(b). In any case in which partial redemption is requested, the phrase "to the extent of \$\_\_\_\_\_ (face amount) and reissue of the remainder" should be added to the request. Upon partial redemption of the bond, the remainder will be reissued as of the original issue date, as provided in Subpart I.

#### § 353.42 Nonreceipt or loss of check issued in payment.

If a check in payment of a bond surrendered for redemption is not received within a reasonable time or is lost after receipt, notice should be given to the same agency to which the bond was surrendered for payment. The notice should give the date the bond was surrendered for payment and describe the bond by series, denomination, serial number, and registration, including the taxpayer identifying number of the owner.

#### § 353.43 Effective date of request for payment.

The Department of the Treasury will treat the receipt of a bond with an appropriate request for payment by (a) a Federal Reserve Bank or Branch, (b) the Bureau of the Public Debt, or (c) a paying agent authorized to pay that bond, as the date upon which the rights of the parties are fixed for the purpose of payment.

#### § 353.44 Withdrawal of request for payment.

(a) *Withdrawal by owner or coowner.* An owner or coowner, who has surrendered a bond to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt or to an authorized paying agent with an appropriate request for payment, may withdraw the request if notice of intent to withdraw is received by the same agency prior to payment either in cash or through the issuance of the redemption check.



(b) *Withdrawal on behalf of deceased owner or incompetent.* A request for payment may be withdrawn under the same conditions as in paragraph (a) of this section by the executor or administrator of the estate of a deceased owner or by the person or persons who could have been entitled to the bond under Subpart L, or by the legal representative of the estate of a person under legal disability, unless surrender of the bond for payment has eliminated the interest of a surviving coowner or beneficiary. See § 353.70(b) and (c).

#### SUBPART I—REISSUE AND DENOMINATIONAL EXCHANGE

##### § 353.45 General.

Reissue of a bond may be made only under the conditions specified in these regulations, and only at (a) a Federal Reserve Bank or Branch, or (b) the Bureau of the Public Debt. Reissue will not be made if the request is received less than one full calendar month before the final maturity date of a bond. The request, however, will be effective to establish ownership as though the requested reissue had been made.

##### § 353.46 Effective date of request for reissue.

The Department of the Treasury will treat the receipt by (a) a Federal Reserve Bank or Branch or (b) the Bureau of the Public Debt of a bond and an acceptable request for reissue as determining the date upon which the rights of the parties are fixed for the purpose of reissue. For example, if the owner or either coowner of a bond dies after the bond has been surrendered for reissue, the bond will be regarded as having been reissued in the decedent's lifetime.

##### § 353.47 Authorized reissue—During lifetime.

A bond belonging to an individual may be reissued in any authorized form of registration upon an appropriate request for the purposes outlined below.

(a) *Single ownership.* A bond registered in single ownership form may be reissued—

(1) To add a coowner or beneficiary; or

(2) To name a new owner, with or without a coowner or beneficiary, but only if (i) the new owner is related to the previous owner by blood (including legal adoption) or marriage; (ii) the previous owner and the new owner are parties to a divorce or annulment; or (iii) the new sole owner is the trustee of a personal trust estate which was created by the previous owner or which designates as beneficiary either the previous owner or a person related to him or her by blood (including legal adoption) or marriage.

(b) *Coownership.* (1) *Reissue—to name a related individual as owner or coowner.* During the lifetime of both coowners, a coownership bond may be reissued in the name of another individual related by blood (including legal adoption) or marriage to either coowner:

(i) As single owner,

(ii) As owner with one of the original coowners as beneficiary, or

(iii) As a new coowner with one of the original coowners.

(2) *Reissue—to name either coowner alone or with another individual as coowner or beneficiary.* During the lifetime of both coowners, a coownership bond may be reissued in the name of either coowner alone or with another individual as coowner or beneficiary if:

(i) After issue of the submitted bond, either coowner named thereon marries, or the coowners are divorced or legally separated from each other, or their marriage is annulled; or

(ii) Both coowners on the submitted bond are related by blood (including legal adoption) or marriage to each other.

(3) *Reissue—to name the trustee of a personal trust estate.* A bond registered in coownership form may be reissued to name a trustee of a personal trust estate created by either coowner or by some other person if (i) either coowner is a beneficiary of the trust, or (ii) a beneficiary of the trust is related by blood or marriage to either coowner.

(c) *Beneficiary.* A bond registered in beneficiary form may be reissued:

(1) To name the beneficiary as coowner;

- (2) To substitute another individual as beneficiary; or
- (3) To eliminate the beneficiary, and, if the beneficiary is eliminated, to effect any of the reissues authorized by paragraph (a) of this section.

#### § 353.48 Restrictions on reissue.

(a) *Denominational exchange.* Reissue is not permitted solely to change denominations.

(b) *United States Treasury.* Reissue may not be made to eliminate the United States Treasury as coowner.

#### § 353.49 Correction of errors.

A bond may be reissued to correct an error in registration upon appropriate request supported by satisfactory proof of the error.

#### § 353.50 Change of name.

An owner, coowner, or beneficiary whose name is changed by marriage, divorce, annulment, order of court, or in any other legal manner after the issue of the bond should submit the bond with a request for reissue to substitute the new name for the name inscribed on the bond. Documentary evidence may be required in any appropriate case.

#### § 353.51 Requests for reissue.

A request for reissue of bonds in coownership form must be signed by both coowners, except that a request solely to eliminate the name of one coowner may be signed by that coowner only. A bond registered in beneficiary form may be reissued upon the request of the owner, without the consent of the beneficiary. Public Debt forms are available for requesting reissue.

### SUBPART J—CERTIFYING OFFICERS

#### § 353.55 Individuals authorized to certify.

The following individuals are authorized to act as certifying officers for the purpose of certifying a request for payment, reissue, or a signature to a Public Debt form:

(a) *Officers generally authorized.* (1) *At banks, trust companies, and member organizations of the Federal Home Loan Bank System.*

(i) Any officer of a bank incorporated in the United States, the territories or possessions of the United States, or the Commonwealth of Puerto Rico.

(ii) Any officer of a trust company incorporated in the United States, the territories or possessions of the United States, or the Commonwealth of Puerto Rico.

(iii) Any officer of an organization that is a member of the Federal Home Loan Bank System. This includes Federal savings and loan associations.

(iv) Any officer of a foreign branch or a domestic branch of an institution indicated in (i) through (iii).

(v) Any officer of a Federal Reserve Bank, a Federal Land Bank, or a Federal Home Loan Bank.

(vi) Any employee of an institution in (i) through (v), who is expressly authorized to certify by the institution.

Certification by these officers or designated employees must be authenticated by a legible imprint of either the corporate seal of the institution or of the issuing or paying agent's stamp. The employee expressly authorized to certify by an institution must sign his or her name over the title "Designated Employee".

(2) *At issuing agents that are not banks or trust companies.* Any officer of an organization, not a bank or a trust company, that is qualified as an issuing agent for bonds of Series EE. The agent's stamp must be imprinted in the certification.

(3) *By United States officials.* Any judge, clerk, or deputy clerk of a United States court, including United States courts for the territories and possessions of the United States and the Commonwealth of Puerto Rico; any United States Commissioner, United States Attorney, or United States Collector of Customs, including their

deputies; in the Internal Revenue Service, any Regional Commissioner, District Director, Service Center Director, or Internal Revenue agent.

(b) *Officers with limited authority.* (1) *In the Armed Forces.* Any commissioned officer or warrant officer of the Armed Forces of the United States, but only for members of the respective services, their families, and civilian employees at posts, bases, or stations. The certifying officer must indicate his or her rank and state that the individual signing the request is one of the class whose request the certifying officer is authorized to certify.

(2) *At the Veterans Administration, Federal penal institutions, and United States Public Health Service hospitals.* Any officer in charge of a home, hospital, or other facility of the Veterans Administration, but only for the patients, or employees of the facility; any officer of a Federal penal institution or a United States Public Health Service hospital expressly authorized to certify by the Secretary of the Treasury or his designee, but only for the inmates, patients or employees of the institution involved. Officers of Veterans Administration facilities, Federal penal institutions, and Public Health Service hospitals must use the stamp or seal of the particular institution or service.

(c) *Authorized officers in foreign countries.* Any United States diplomatic or consular representative, or the officer of a foreign branch of a bank or trust company incorporated in the United States whose signature is attested by an imprint of the corporate seal or is certified to the Department of the Treasury. If none of these individuals is available, a notary public or other officer authorized to administer oaths may certify, but his or her official character and jurisdiction must be certified by a United States diplomatic or consular officer under seal of his or her office.

(d) *Authorized officers in particular localities.* The Governor and the Treasurer of Puerto Rico; the Governor and the Commissioner of Finance of the Virgin Islands; the Governor and the Director of Finance of Guam; the Governor and the Director of Administrative Services of American Samoa; or designated officers of the Panama Canal Commission.

(e) *Special provisions.* If no certifying officer is readily accessible, the Commissioner of the Public Debt, Deputy Commissioner, any Assistant Commissioner, or other designated official of the Bureau or of a Federal Reserve Bank or Branch is authorized to make special provision for any particular case.

### **§ 353.56 General instructions and liability.**

(a) The certifying officer must:

(1) Require the person presenting a bond, or an appropriate Public Debt transaction form, to establish his or her identity in accordance with Department of the Treasury instructions and identification guidelines;

(2) Place a notation on the back of the bond or on the appropriate Public Debt transaction form, or in a separate record, showing exactly how identification was established; and

(3) Affix, as part of the certification, his or her official signature, title, seal or issuing or paying agent's stamp, address, and the date of execution.

(b) The certifying officer and, if such person is an officer or an employee of an organization, the organization will be held fully responsible for the adequacy of the identification.

### **§ 353.57 When a certifying officer may not certify.**

Certifying officers may not certify the requests for payment of bonds, or appropriate Public Debt transaction forms if, in their own right or in a representative capacity, they—

(a) Have an interest in the bonds, or

(b) Will, by virtue of the requests being certified, acquire an interest in the bonds.

### **§ 353.58 Forms to be certified.**

When required in the instructions on a Public Debt transaction form, the form must be signed before an authorized certifying officer.



## SUBPART K—MINORS, INCOMPETENTS, AGED PERSONS, ABSENTEES, ET AL.

**§ 353.60 Payment to representative of an estate.**

(a) The representative of an estate of an owner who is a minor, an aged person, incompetent, absentee, et al., may receive payment upon request:

- (1) If the registration shows the name and capacity of the representative;
- (2) If the registration shows the capacity but not the name of the representative and the request is accompanied by appropriate evidence; or
- (3) If the registration includes neither the name of the representative nor his or her capacity but the request is accompanied by appropriate evidence.

(b) Appropriate evidence for paragraphs (a)(2) and (a)(3) of this section includes a certified copy of the letters of appointment or, if the representative is not appointed by a court, other proof of qualification. Except in the case of corporate fiduciaries, the evidence must show that the appointment is in full force and be dated not more than one year prior to the presentation of the bond for payment. The request for payment appearing on the back of a bond must be signed by the representative as such, for example, "John S. Jones, guardian (committee) of the estate of Henry W. Smith, a minor (an incompetent)".

**§ 353.61 Payment after death.**

After the death of the ward, and at any time prior to the representative's discharge, the representative of the estate will be entitled to obtain payment of a bond to which the ward was solely entitled.

**§ 353.62 Payment to minors.**

If the owner of a savings bond is a minor and the form of registration does not indicate that there is a representative of the minor's estate, payment will be made to the minor upon his or her request, provided the minor is of sufficient competency to sign the request for payment and to understand the nature of the transaction. In general, the fact that the request for payment has been signed by a minor and certified will be accepted as sufficient proof of competency and understanding.

**§ 353.63 Payment to a parent or other person on behalf of a minor.**

If the owner of a savings bond is a minor and the form of registration does not indicate that there is a representative of his or her estate, and if the minor is not of sufficient competency to sign the request for payment and to understand the nature of the transaction, payment will be made to either parent with whom the minor resides or to whom legal custody has been granted. If the minor does not reside with either parent, payment will be made to the person who furnishes the chief support for the minor. The request must appear on the back of the bond in one of the following forms:

**(a) Request by parent.**

I certify that I am the mother of John C. Jones (with whom he resides) (to whom legal custody has been granted). He is \_\_\_\_\_ years of age and is not of sufficient understanding to make this request.

Mary Jones on behalf of John C. Jones.

**(b) Request by other person.**

I certify that John C. Jones does not reside with either parent and that I furnish his chief support. He is \_\_\_\_\_ years of age and is not of sufficient understanding to make this request.

Alice Brown, grandmother, On behalf of John C. Jones.

**§ 353.64 Payment, reinvestment, or exchange—Voluntary guardian of an incompetent.**

When an adult owner of bonds is incapable of requesting payment and there is no other person legally qualified to do so, the relative or other person responsible for the owner's care and support may submit an application for recognition as voluntary guardian for the purpose of redeeming the bonds in the following situations:

- (a) The proceeds of the bonds are needed to pay expenses already incurred, or to be incurred during a 90-day period, for the support of the incompetent or his or her legal dependents.

(b) If the bonds have finally matured and it is desired to redeem them and reinvest the proceeds in other savings bonds, the new bonds must be registered in the name of the incompetent, followed by words showing he or she is under voluntary guardianship; for example, "John Jones 123-45-6789, under voluntary guardianship". A living coowner or beneficiary named on the matured bonds must be designated on the new bonds unless the named person furnishes a certified statement consenting to omission of his or her name. If an amount insufficient to purchase an additional bond of any authorized denomination of either series remains after the reinvestment, the voluntary guardian may furnish additional funds sufficient to purchase another bond of either series in the lowest available denomination. If additional funds are not furnished, the remaining amount will be paid to the voluntary guardian for the use and benefit of the incompetent. The provisions for reinvestment of the proceeds of matured bonds are equally applicable to any authorized exchange of bonds of one series for those of another.

#### **§ 353.65 Payment—Attorney-in-fact of an incompetent or a physically disabled person.**

A request for payment by an individual as attorney-in-fact of an incompetent or a physically disabled owner will be honored if the power of attorney grants the attorney-in-fact authority to sell or redeem the grantor's securities, sell his or her personal property, or otherwise grants similar authority. The power of attorney must provide that the grantor's subsequent incapacity will not affect the authority granted. The request must be supported by a copy of the power of attorney and evidence of the incapacity of the grantor.

#### **§ 353.66 Reissue.**

A bond on which a minor or other person under legal disability is named as the owner or coowner, or in which he or she has an interest, may be reissued under the following conditions:

(a) A minor for whose estate no representative has been appointed may request reissue if the minor is of sufficient competency to sign his or her name to the request and to understand the nature of the transaction.

(b) A bond on which a minor is named as beneficiary or coowner may be reissued in the name of a custodian for the minor under a statute authorizing gifts to minor upon the request of the adult whose name appears on the bond as owner or coowner.

(c) A minor coowner for whose estate no representative has been appointed, may be named sole owner upon the request of the competent coowner.

(d) Reissue to eliminate the name of a minor or incompetent for whose estate a legal representative has been appointed is permitted only if supported by evidence that a court has authorized the representative of the minor's or incompetent's estate to request the reissue. See § 353.23.

Except to the extent provided in paragraphs (a) through (d), above, reissue will be restricted to a form of registration which does not adversely affect the existing ownership or interest of a minor who is not of sufficient understanding to make a request, or other person under legal disability. Requests for reissue should be executed by the person authorized to request payment under §§ 353.60 and 353.63, or the person who may request recognition as voluntary guardian under § 353.64.

### **SUBPART L—DECEASED OWNER, COOWNER OR BENEFICIARY**

#### **§ 353.70 General rules governing entitlement.**

The following rules govern ownership or entitlement where one or both of the persons named on a bond have died without the bond having been surrendered for payment or reissue:

(a) *Single owner bond.* If the owner of a bond registered in single ownership form has died, the bond becomes the property of that decedent's estate, and payment or reissue will be made as provided in this Subpart.

(b) *Coowner bond.* (1) *One coowner deceased.* If one of the coowners named on a bond has died, the surviving coowner will be recognized as the sole and absolute owner, and payment or reissue will be made as though the bond were registered in the name of the

survivor alone. Any request for reissue by the surviving coowner must be supported by proof of death of the other coowner.

(2) *Both coowners deceased.* If both coowners named on a bond have died, the bond becomes the property of the estate of the coowner who died last, and payment or reissue will be made as if the bond were registered in the name of the last deceased coowner alone. Proof of death of both coowners will be required to establish the order of death.

(3) *Simultaneously death of both coowners.* If both coowners die under conditions where it cannot be established, either by presumption of law or otherwise, which coowner died first, the bond becomes the property of both equally, and payment or reissue will be made accordingly.

(c) *Beneficiary bond.* (1) *Owner deceased.* If the owner of a bond registered in beneficiary form has died and is survived by the beneficiary, upon proof of death of the owner, the beneficiary will be recognized as the sole and absolute owner of the bond. Payment or reissue will be made as though the bond were registered in the survivor's name alone. A request for payment or reissue by the beneficiary must be supported by proof of death of the owner.

(2) *Beneficiary deceased.* If the beneficiary's death occurs before, or simultaneously with, that of the registered owner, payment or reissue will be made as though the bond were registered in the owner's name alone. Proof of death of the owner and beneficiary is required to establish the order of death.

(d) *Nonresident aliens.* If the person who becomes entitled to a bond because of the death of an owner is an alien who is a resident of an area with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States or its agencies or instrumentalities, delivery of the redemption check will not be made so long as the restriction applies. See Department of the Treasury Circular No. 655, current revision (31 CFR Part 211).

### § 353.71 Estate administered.

(a) *During administration.* The legal representative of an estate may request payment of bonds, including interest or redemption checks, belonging to the estate or may have the bonds reissued in the names of the persons entitled to share in the estate under the following conditions:

(1) When there is more than one legal representative, all must join in the request for payment or reissue, unless § 353.75(a)(1) or (b) applies.

(2) The request for payment or reissue must be signed in the form: "John A. Jones, administrator of the estate (or executor of the will) of Henry M. Jones, deceased". The request must be supported by evidence of the legal representative's authority in the form of a court certificate or a certified copy of the legal representative's letters of appointment which must be dated within six months of the date of presentation of the bond, unless the evidence shows that the appointment was made within one year prior to the presentation of the bond.

(3) For reissue, the legal representative must certify that each person in whose name reissue is requested is entitled to the extent specified and must certify that each person has consented to the reissue. If a person in whose name reissue is requested desires to name a coowner or beneficiary, the person must execute an additional request for reissue on the appropriate form.

(b) *After administration.* If the estate of the decedent has been settled through judicial proceedings, the bond and interest and redemption checks will be paid, or the bond will be reissued, upon the request of the person shown to be entitled by the court order. The request must be supported by a certified copy of the legal representative's court-approved final account, the decree of distribution, or other pertinent court records. If two or more persons have an interest in the bond, they must enter into an agreement concerning the bond's disposition. If the person entitled desires to name a coowner or beneficiary, a separate request must be made on an appropriate form.

(c) *Special provisions for small amounts.* Special procedures are available for establishing entitlement to, or effecting disposition of, savings bonds and interest and redemption checks if the aggregate face amount, excluding interest checks, does not exceed \$1,000.



**§ 353.72 Estate not administered.**

(a) *Special State law provisions.* A request for payment or reissue of a bond by the person who has qualified under State law to receive or distribute the assets of a decedent's estate will be accepted, provided evidence of the person's authority is submitted.

(b) *Agreement of persons entitled.* If there is no legal representative for the estate of a decedent, the bonds will be paid to, or reissued in the name of, the persons entitled, pursuant to an agreement and request executed by all persons entitled to share in the decedent's personal estate. If the persons entitled to share in the decedent's personal estate include minors or incompetents, payment or reissue of the bonds must be made to them or in their names unless their interest in the bonds is otherwise protected.

(c) *Creditors.* An institutional creditor of a deceased owner's estate is entitled to payment only to the extent of its claim.

(d) *Special provisions for payment of small amounts-survivors of the decedent.* (1) If the face amount of the bond does not exceed \$500 and there is no legal representative of the deceased owner's estate, the bond will be paid upon the request of the person who paid the burial expenses and who has not been reimbursed.

(2) If there is no legal representative of the estate of a decedent who died without a will, and total face amount of bonds in the estate does not exceed \$1,000 (face amount), the bonds may be paid to the decedent's survivors upon request in the following order of precedence:

- (i) Surviving spouse;
- (ii) If no surviving spouse, to the child or children of the decedent, and the descendants of deceased children by representation;
- (iii) If none of the above, to the parents of the decedent, or the survivor;
- (iv) If none of the above, to the brothers and sisters, and the descendants of deceased brothers or sisters by representation;
- (v) If none of the above, to other next-of-kin, as determined by the laws of the owner's domicile at death;
- (vi) If none of the above, to persons related to the decedent by marriage.

The payment pursuant to this subsection shall be made upon the request and agreement of the survivors to receive the redemption proceeds individually and for the account of any persons entitled. Interest checks held for the estate of a decedent will be distributed with the bonds.

**SUBPART M—FIDUCIARIES****§ 353.75 Payment or reissue during the existence of the fiduciary estate.**

(a) *Payment or reissue before maturity.* (1) *Request from the fiduciary named in the registration.* A request for reissue or payment prior to maturity must be signed by all of the fiduciaries unless by statute, decree of court, or the terms of the governing instrument, any lesser number may properly execute the request. If the fiduciaries named in the registration are still acting, no further evidence will be required. In other cases, evidence to support the request will be required, as specified:

(i) *Fiduciaries by title only.* If the bond is registered only in the titles, without the names, of fiduciaries not acting as a board, satisfactory evidence of their incumbency must be furnished, except in the case of bonds registered in the title of public officers as trustees.

(ii) *Boards, committees, commission, etc.* If a bond is registered in the name of a governing body which is empowered to act as a unit, and which holds title to the property of a religious, educational, charitable or nonprofit organization or a public corporation, the request should be signed in the name of the body by an authorized person. Ordinarily, a signed and certified request will be accepted without further evidence.

(iii) *Corporate fiduciaries.* If a bond is registered in the name of a public or private corporation or a governmental body as fiduciary, the request must be signed by an authorized officer in the name of the organization as fiduciary. Ordinarily, a signed and certified request will be accepted without further evidence.

(2) *Trustee of a common trust fund.* A bond held by a financial institution in a fiduciary capacity may be reissued in the name of the institution as trustee of its common trust fund to the extent that participation in the common trust fund is authorized by law or regulation. The request for reissue should be executed by the institution and any cofiduciary.

(3) *Successor fiduciary.* If the fiduciary in whose name the bond is registered has been replaced by another fiduciary, satisfactory evidence of successorship must be furnished.

(b) *Payment at or after final maturity.* At or after final maturity, a request for payment signed by any one or more of the fiduciaries will be accepted.

Payment will be made by check drawn as the bond is registered.

#### **§ 353.76 Payment or reissue after termination of the fiduciary estate.**

A bond registered in the name or title of a fiduciary may be paid or reissued to the person who has become entitled by reason of the termination of a fiduciary estate. Requests for reissue made by a fiduciary pursuant to the termination of a fiduciary estate should be made on the appropriate form. Requests for payment or reissue by other than the fiduciary must be accompanied by evidence to show that the person has become entitled in accordance with applicable State law or otherwise. When two or more persons have become entitled, the request for payment or reissue must be signed by each of them.

#### **§ 353.77 Exchanges by fiduciaries.**

Fiduciaries are authorized to request an exchange of bonds of one series for those of another, pursuant to any applicable Department of the Treasury offering. A living coowner or beneficiary named on the bonds submitted in exchange may be retained in the same capacity on the new bonds.

### **SUBPART N—PRIVATE ORGANIZATIONS (CORPORATIONS, ASSOCIATIONS, PARTNERSHIPS, ET CETERA) AND GOVERNMENTAL AGENCIES, UNITS AND OFFICERS**

#### **§ 353.80 Payment to corporations or unincorporated associations.**

A bond registered in the name of a private corporation or an unincorporated association will be paid to the corporation or unincorporated association upon a request for payment on its behalf by an authorized officer. The signature to the request should be in the form, for example, "The Jones Coal Company, a corporation, by John Jones, President", or "The Lotus Club, an unincorporated association, by William A. Smith, Treasurer". A request for payment so signed and certified will ordinarily be accepted without further evidence of the officer's authority.

#### **§ 353.81 Payment to partnerships.**

A bond registered in the name of an existing partnership will be paid upon a request for payment signed by a general partner. The signature to the request should be in the form, for example, "Smith and Jones, a partnership, by John Jones, a general partner". A request for payment so signed and certified will ordinarily be accepted as sufficient evidence that the partnership is still in existence and that the person signing the request is authorized.

#### **§ 353.82 Reissue or payment to successors of corporations, unincorporated associations, or partnerships.**

A bond registered in the name of a private corporation, an unincorporated association, or a partnership which has been succeeded by another corporation, unincorporated association, or partnership by operation of law or otherwise, in any manner whereby the business or activities of the original organization are continued without substantial change, will be paid to or reissued in the name of the succeeding organization upon appropriate request on its behalf, supported by satisfactory evidence of successorship. The appropriate form should be used.

**§ 353.83 Reissue or payment on dissolution of corporation or partnership.**

(a) *Corporations.* A bond registered in the name of a private corporation which is in the process of dissolution will be paid to the authorized representative of the corporation upon a request for payment, supported by satisfactory evidence of the representative's authority. At the termination of dissolution proceedings, the bond may be reissued upon the request of the authorized representative in the names of those persons, other than creditors, entitled to the assets of the corporation, to the extent of their respective interests. Proof will be required that all statutory provisions governing the dissolution of the corporation have been complied with and that the persons in whose names reissue is requested are entitled and have agreed to the reissue. If the dissolution proceedings are under the direction of a court, a certified copy of an order of the court, showing the authority of the representative to make the distribution requested must be furnished.

(b) *Partnerships.* A bond registered in the name of a partnership which has been dissolved by death or withdrawal of a partner, or in any other manner:

(1) Will be paid upon a request for payment by any partner or partners authorized by law to act on behalf of the dissolved partnership, or

(2) Will be paid to or reissued in the names of the persons entitled as the result of such dissolution to the extent of their respective interests, except that reissue will not be made in the names of creditors. The request must be supported by satisfactory evidence of entitlement, including proof that the debts of the partnership have been paid or properly provided for. The appropriate form should be used.

**§ 353.84 Payment to certain institutions.**

A bond registered in the name of a church, hospital, home, school, or similar institution, without reference in the registration to the manner in which it is organized or governed or to the manner in which title to its property is held, will be paid upon a request for payment signed on behalf of such institution by an authorized representative. A request for payment signed by a pastor of a church, superintendent of a hospital, president of a college, or by any official generally recognized as having authority to conduct the financial affairs of the particular institution will ordinarily be accepted without further proof of authority. The signature to the request should be in the form, for example, "Shriners' Hospital for Crippled Children, St. Louis, Missouri, by William A. Smith, Superintendent", or "St. Mary's Roman Catholic Church, Albany, New York, by the Rev. John Smyth, Pastor".

**§ 353.85 Reissue in name of trustee or agent for reinvestment purposes.**

A bond registered in the name of a religious, educational, charitable or nonprofit organization, whether or not incorporated, may be reissued in the name of a financial institution, or an individual, as trustee or agent. There must be an agreement between the organization and the trustee or agent holding funds of the organization, in whole or in part, for the purpose of investing and reinvesting the principal and paying the income to the organization. Reissue should be requested on behalf of the organization by an authorized officer using the appropriate form.

**§ 353.86 Reissue upon termination of investment agency.**

A bond registered in the name of a financial institution, or individual, as agent for investment purposes only, under an agreement with a religious, an educational, a charitable, or a nonprofit organization, may be reissued in the name of the organization upon termination of the agency. The former agent should request such reissue and should certify that the organization is entitled by reason of the termination of the agency. If such request and certification are not obtainable, the bond will be reissued in the name of the organization upon its own request, supported by satisfactory evidence of the termination of the agency. The appropriate form should be used.

**§ 353.87 Payment to governmental agencies, units, or their officers.**

(a) *Agencies and units.* A bond registered in the name of a State, county, city, town, village, or in the name of a Federal, State, or local governmental agency, such as a board, commission, or corporation, will be paid upon a request signed in the name of



the governmental agency or unit or by an authorized officer. A request for payment so signed and certified will ordinarily be accepted without further proof of the officer's authority.

(b) *Officers.* A bond registered in the official title of an officer of a governmental agency or unit will be paid upon a request for payment signed by the officer. The request for payment so signed and certified will ordinarily be accepted as proof that the person signing is the incumbent of the office.

#### SUBPART O—MISCELLANEOUS PROVISIONS

##### § 353.90 Waiver of regulations.

The Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may waive or modify any provision or provisions of these regulations. He may do so in any particular case or class of cases for the convenience of the United States or in order to relieve any person or persons of unnecessary hardship, (a) if such action would not be inconsistent with law or equity, (b) if it does not impair any existing rights, and (c) if he is satisfied that such action would not subject the United States to any substantial expense or liability.

##### § 353.91 Additional requirements; bond of indemnity.

The Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may require (a) such additional evidence as he may consider necessary or advisable, or (b) a bond of indemnity, with or without surety, in any case in which he may consider such a bond necessary for the protection of the interests of the United States.

##### § 353.92 Supplements, amendments, or revisions.

The Secretary of the Treasury may at any time, or from time to time, prescribe additional, supplemental, amendatory, or revised rules and regulations governing United States Savings Bonds of Series EE and HH.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

#### Exhibit 8.—Department Circular No. 26-76, regulations governing book-entry Treasury bills, First Amendment

DEPARTMENT OF THE TREASURY,  
*Washington, January 10, 1980.*

**SUMMARY:** On December 13, 1979, the Department of the Treasury published for comment a proposed amendment of the regulations governing book-entry Treasury bills (31 CFR, Part 350) to increase the period prior to maturity during which requests for transactions affecting book-entry accounts maintained by the Bureau of the Public Debt would not be accepted.

No responses were received during the period reserved for filing written comments, which expired on January 4, 1980. An earlier opportunity to file comments on this amendment had been provided, i.e., during the period from August 23 to October 19, 1979. A republication of the amendment was made because of a clerical error that had appeared in the notice published in the Federal Register on August 23, 1979. No comments to that earlier notice were received.

**EFFECTIVE DATE:** January 15, 1980.

Section 350.8 is amended as set forth below:

\* \* \* \* \*

##### Sec. 350.8 Transfer.

Book-entry Treasury bills maintained under this subpart may not be transferred from one account maintained by the Treasury to another such account, except in cases of lawful succession, as provided in this subpart. They may be withdrawn from an

account maintained by the Treasury hereunder and transferred through the Federal Reserve Bank communication system to an account maintained by or through a member bank under Subpart B, which transfer shall be made in the name or names appearing in the account recorded on the books of the Treasury. Such withdrawal may be effected by a certified request therefor by, or on behalf of, the depositor, provided the request therefor is received no earlier than twenty (20) business days after the issue date or the date the securities are transferred to the Treasury, whichever is later, or no later than twenty (20) business days before the maturity date. The request must: (a) identify the book-entry account by the name of the depositor and title, if any, the address, and the taxpayer identifying number; (b) specify by amount, maturity date and CUSIP number the book-entry Treasury bills to be withdrawn and transferred; and (c) specify the name of the member bank to or through which the transfer is to be effected and, where appropriate, the name of the institution or entity which is to maintain the book-entry account. In the case of book-entry Treasury bills held in the names of two individuals, a certified request by either will be accepted, but the transfer shall be made in the names of both. A transfer after original issue of book-entry Treasury bills from an account maintained by or through a member bank to one maintained by the Treasury may be made through the Federal Reserve Bank communication system, provided the account is to be held in a form authorized by this subpart, and provided the transfer is made no later than one month prior to the maturity date of the bills.

\* \* \* \* \*

Section 350.14 is amended by revising paragraph (a) as set forth below:

\* \* \* \* \*

#### **Sec. 350.14 Reinvestment or payment at maturity.**

(a) *Request for reinvestment.* Upon the request of the depositor in whose name the account is maintained, book-entry Treasury bills held therein will be reinvested at maturity, i.e., their proceeds at maturity will be applied to the purchase of new Treasury bills at the average price (in three decimals) of accepted competitive bids for such Treasury bills then being offered. The request for a reinvestment may be made on the tender form at the time of purchase; subsequent requests for reinvestment will be accepted if received by the Bureau no later than twenty (20) business days prior to the maturity of the bills. The difference between the par value of the maturing bills and the issue price of the new bills will be remitted to the subscriber in the form of a Treasury check. Requests for the revocation of the reinvestment of bills will also be accepted if received no later than twenty (20) business days prior to the maturity date.

\* \* \* \* \*

Section 350.16 is amended by revising paragraph (a) as set forth below:

\* \* \* \* \*

#### **Sec. 350.16 Transactions in regular course—notices not effective—unacceptable notices.**

(a) *Transactions in regular course—notices not effective.* Transfers of book-entry Treasury bills, payment thereof or reinvestment at maturity or any other transaction therein will be conducted in the regular course of business in accordance with this subpart, notwithstanding notice of the appointment of an attorney-in-fact, or a legal guardian or similar representative, or notice of successorship, the termination of an estate, the dissolution of an entity, or the death of an individual, unless the requisite request, proof, and the evidence necessary to establish entitlement under this subpart is

received by the Bureau no later than twenty (20) business days prior to the maturity date of the bills.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 9.—Department Circular No. 905, Seventh Revision, offering of United States savings bonds, Series H**

DEPARTMENT OF THE TREASURY,  
*Washington, January 2, 1980.*

**SUMMARY:** This Seventh Revision of the offering circular for United States Savings Bonds, Series H, i.e., Department of the Treasury Circular No. 905, shows the improvements in the investment yields of Series H bonds. It also makes other changes in the terms of the offering necessitated by the termination of the sale of these bonds on December 31, 1979.

**EFFECTIVE DATE:** June 1, 1979.

**SUPPLEMENTAL INFORMATION:** On May 10, 1979, the Secretary of the Treasury announced that the interest rate paid on Series H savings bonds would be increased, effective June 1, 1979, to 6.5 percent per annum, compounded semiannually, if held to maturity. This revision of the offering circular for Series H bonds effectuates this increase and provides tables of interest payments and investment yields which reflect the higher rate.

As provided in the revision, this rate increase of  $\frac{1}{2}$  of 1 percent per annum is applied as follows:

First, Series H bonds purchased on and after June 1, 1979, will have an investment yield of 6.5 percent per annum, compounded semiannually, if held to original maturity, ten years from issue date. If the bond is redeemed before original maturity, the yield will be less than 6.5 percent.

Second, bonds issued prior to June 1, 1979, whether they are now in their original maturity period or an extended maturity period, will receive a  $\frac{1}{2}$  percent increase in investment yield to their original or next maturity date. The increase will be included in the interest check for the semiannual interest period that begins on or after June 1, 1979, and for each semiannual interest period thereafter.

*For example:* For a bond bearing an issue date of September 1, 1964, its first semiannual interest period after June 1, 1979, began on September 1, 1979. The interest check for that period, which will be issued on March 1, 1980, will be the first check that will reflect the improved yield.

In addition to effectuating the rate increase, this revision of the Series H bond offering circular includes several other changes relating to the termination of sale of the bonds, as announced by the Secretary of the Treasury on January 10, 1979.

First, § 332.1 provides that the offering of Series H bonds will terminate on December 31, 1979.

Second, § 332.8, relating to the extended maturity periods granted to Series H bonds, is revised. The term "extended maturity period" refers to one or more ten-year periods during which Series H bonds, if not sooner redeemed, continue to earn interest after the end of their original maturity period.

In accordance with the Secretary's prior announcement, Series H bonds bearing issue dates of June 1, 1952, through May 1, 1959, which have already been granted two 10-year extensions, will not be extended again. Thus, Series H bonds issued from June 1, 1952, to January 1, 1957, will reach final maturity 29 years, 8 months, from their respective issue dates and will cease to earn interest at that time. Series H bonds issued from February 1, 1957, to May 1, 1959, will reach final maturity exactly 30 years from their respective issue dates. All Series H bonds issued after May 1, 1959, are granted a second 10-year extension.

Finally, several minor changes have been made to the offering to update addresses used in connection with Series H bond transactions.



\* \* \* \* \*

Accordingly, Department of the Treasury Circular No. 905, Sixth Revision, dated April 19, 1974, as amended and supplemented, including the tables incorporated therein (31 CFR, Part 332), is hereby revised and reissued as Department of the Treasury Circular No. 905, Seventh Revision, effective as of June 1, 1979.

This revision is effected under authority of Section 22 of the Second Liberty Bond Act, as amended (49 Stat. 21, as amended; 31 U.S.C. 757c) and 5 U.S.C. 301. Since this revision involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures thereon are unnecessary.

## PART 332—OFFERING OF U.S. SAVINGS BONDS, SERIES H

Authority: Sec. 22, Second Liberty Bond Act as amended, 49 Stat. 21, as amended, (31 U.S.C. 757c) and (5 U.S.C. 301).

### § 332.1 Offering of bonds.

The Secretary of the Treasury hereby offers for sale to the people of the United States, United States Savings Bonds of Series H, hereinafter generally referred to as "Series H bonds" or "bonds". This offer, effective as of June 1, 1979, will terminate on December 31, 1979.

### § 332.2 Description of bonds.

(a) *General.* Series H bonds bear a facsimile of the signature of the Secretary of the Treasury and of the Seal of the Department of the Treasury. They are issued only in registered form and are nontransferable.

(b) *Denominations and prices.* Series H bonds are issued at face (par) amount and are available in denominations of \$500, \$1,000, \$5,000 and \$10,000.

(c) *Inscription and issue.* At the time of issue the issuing agent will (1) inscribe on the face of each bond the name, social security number and address of the owner, and the name of the beneficiary, if any, or the name, social security number and address of the first-named coowner and the name of the other coowner; (2) enter in the upper right-hand portion of the bond the issue date; and (3) imprint the agent's dating stamp in the lower right-hand portion to show the date the bond is actually inscribed. A bond shall be valid only if an authorized issuing agent receives payment therefor and duly inscribes, dates and stamps it.

(d) *Term.* A Series H bond shall be dated as of the first day of the month in which payment therefor is received by an agent authorized to issue the bond. This date is the issue date and the bond will mature and be payable 10 years thereafter. The bond may not be called for redemption by the Secretary of the Treasury prior to maturity or the end of any extended maturity period (see § 332.8(a)(1)). The bond may be redeemed at par after six months from issue date.

(e) *Investment yield (interest).* The interest on a Series H bond will be paid semiannually by check drawn to the order of the registered owner or coowners, beginning six months from the issue date. Interest payments will be on a graduated scale, fixed to produce an investment yield of approximately 6.5 percent per annum, compounded semiannually, if the bond is held to maturity, but the yield will be less if the bond is redeemed prior thereto. See Table 56. Interest will cease at the end of the final authorized extended maturity period, or if redeemed earlier, at the end of the interest period next preceding the date of redemption. However, if the date of redemption falls on an interest payment date, interest will cease on that date.

### § 332.3 Governing regulations.

Series H bonds are subject to the regulations of the Department of the Treasury, now or hereafter prescribed governing United States Savings Bonds (of Series A, B, C, D, E, F, G, H, J and K), contained in Department of the Treasury Circular No. 530, current revision (31 CFR, Part 315),<sup>1</sup> except as otherwise specifically provided herein.

<sup>1</sup> Copies may be obtained from any Federal Reserve Bank or Branch, from the Bureau of the Public Debt, Washington, D.C. 20226, or from the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101.

### § 332.4 Registration.

(a) *General.* Generally, only residents of the United States, its territories and possessions, the Commonwealth of Puerto Rico, and citizens of the United States temporarily residing abroad are eligible to be named as owners of Series H bonds. The bonds may be registered in the names of natural persons in their own right, as provided in paragraph (b) of this section, and in the names and titles or capacities of fiduciaries and organizations, as provided in paragraph (c) of this section. Full information regarding authorized forms of registration and restrictions with respect thereto are found in the governing regulations.

(b) *Natural persons in their own right.* The bonds may be registered in the names of natural persons (whether adults or minors) in their own right, in single ownership, coownership, and beneficiary forms.

(c) *Others.* The bonds may be registered in single ownership form in the names of fiduciaries and private and public organizations, as follows:

(1) *Fiduciaries.* In the names of and showing the titles or capacities of any persons or organizations, public or private, as fiduciaries (including trustees, legal guardians or similar representatives, and certain custodians), but not where the fiduciary would hold the bonds merely or principally as security for the performance of a duty, obligation or service.

(2) *Private and public organizations.* In the names of private or public organizations (including private corporations, partnerships, and unincorporated associations, and States, counties, public corporations, and other public bodies) in their own right, but not in the names of commercial banks.<sup>2</sup>

### § 332.5 Limitation on holdings.

The amount of Series H bonds originally issued during any one calendar year that may be held by any one person, at any one time, computed in accordance with the governing regulations, is limited as follows:

(a) *General limitation.* \$10,000 (face amount) for the calendar year 1974 and each calendar year thereafter.

(b) *Special limitation for gifts to exempt organizations under 26 CFR 1.501(c)(3)-1.* \$200,000 (face amount) for bonds received as gifts by an organization which at the time of purchase is an exempt organization under the terms of 26 CFR 1.501(c)(3)-1.

(c) *Exchange pursuant to Department of the Treasury Circular No. 1036, as amended.* Series H bonds issued in an exchange pursuant to the provisions of Department of the Treasury Circular No. 1036 (31 CFR Part 339) are exempt from the annual limitation.

### § 332.6 Purchase of bonds.

(a) *Issuing Agents.* Only the Federal Reserve Banks and Branches and the Department of the Treasury are authorized to act as issuing agents for the sale of Series H bonds. However, financial institutions may forward applications for purchase of the bonds. The date an issuing agent receives the application and payment will govern the issue date of the bond purchased.

(b) *Application for purchase and remittance.* The applicant for purchase of Series H bonds should furnish (1) instructions for registration of the bonds to be issued, which must be in an authorized form; (2) the appropriate social security or employer identification number; (3) the post office address of the owner or first-named coowner; and (4) the address(es) for delivery of the bonds and for mailing checks in payment of interest, if other than that of the owner or first-named coowner. The application should be forwarded to a Federal Reserve Bank or Branch, or the Department of the Treasury, Washington, D.C. 20226, accompanied by a remittance to cover the purchase price. Any form of exchange, including personal checks, will be accepted subject to collection. Checks or other forms of exchange should be drawn to the order of the Federal Reserve Bank or the United States Treasury, as the case may be. Checks payable by endorsement are not acceptable. Any depository qualified pursuant to Department of the Treasury Circular No. 92, current revision (31 CFR, Part 203), will be permitted to make payment by credit for bonds applied for on behalf of its

<sup>2</sup>For this purpose, commercial banks (as defined in § 315.7, Department of the Treasury Circular No. 530, current revision) are those accepting demand deposits.

customers up to any amount for which it shall be qualified in excess of existing deposits when so notified by the Federal Reserve Bank of its district.

### § 332.7 Delivery of bonds.

Authorized issuing agents will deliver Series H bonds either over-the-counter in person, or by mail at the risk and expense of the United States, to the address given by the purchaser, but only within the United States, its territories and possessions, and the Commonwealth of Puerto Rico. No mail deliveries elsewhere will be made. If purchased by citizens of the United States temporarily residing abroad, the bonds will be delivered at such address in the United States as the purchaser directs.

### § 332.8 Extended terms and improved yields for outstanding bonds.

(a) *Extended maturity periods*—(1) *General*. The terms “extended maturity period” and “second extended maturity period”, when used herein, refer to 10-year intervals after the original maturity dates during which owners may retain their bonds and continue to earn interest thereon. No special action is required of owners desiring to take advantage of any extensions heretofore or herein granted.<sup>3</sup>

(2) *Two extensions*. All Series H bonds may be retained for two extended maturity periods of 10 years each.

(b) *Improved yields*<sup>4</sup> —*Outstanding bonds*. The investment yield on all outstanding Series H bonds is hereby increased as follows:

(1) *Bonds reaching original maturity period on or after December 1, 1979*. By approximately  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, to original maturity, on or after December 1, 1979, the increase to be included in the interest checks issued on or after that date.

(2) *Bonds which entered an extended maturity period prior to December 1, 1979*. By approximately  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, for the remaining period to their next maturity date. The increase will be included in the interest checks issued on or after December 1, 1979.

(3) *Other extensions*. The investment yield for any authorized extensions, other than as set forth in paragraphs (b) (1) or (2) of this section, will be at the rate of 6.5 percent per annum, compounded semiannually, unless such rate is changed prior to the commencement of the extension period. If a change in rate is made, the tables of redemption values and investment yields published herein for such extensions shall not apply.

### § 332.9 Taxation

The income derived from Series H bonds is subject to all taxes imposed under the Internal Revenue Code of 1954. The bonds are subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority.

### § 332.10 Payment or redemption.

A Series H bond may be redeemed at par at any time after six months from the issue date. The bond must be presented and surrendered, with a duly executed request for payment, to (a) a Federal Reserve Bank or Branch, (b) the Department of the Treasury, Washington, D.C. 20226, or (c) the Bureau of the Public Debt, Parkersburg, West Virginia 26101. A bond received by an agent during the calendar month preceding an interest payment date may not be redeemed until that date.

### § 332.11 Reservation as to issue of bonds.

The Secretary of the Treasury reserves the right to reject any application for Series H bonds, in whole or in part, and to refuse to issue or permit to be issued hereunder

<sup>3</sup> The tables incorporated herein, arranged according to issue dates, show current schedules of interest payments and investment yields. (Not included in this exhibit but may be found in the Federal Register, Jan. 2, 1980.)

<sup>4</sup> See Appendix for summary of investment yields to maturity, extended maturity and second extended maturity dates under regulations heretofore and herein prescribed.



any such bonds in any case or any class or classes of cases if he deems such action to be in the public interest, and his action in any such respect shall be final.

**§ 332.12 Preservation of rights.**

Nothing contained herein shall limit or restrict rights which owners of Series H bonds heretofore issued have acquired under offers previously in force.

**§ 332.13 Fiscal agents.**

Federal Reserve Banks and Branches, as fiscal agents of the United States, are authorized to perform such services as may be requested of them by the Secretary of the Treasury in connection with the issue, delivery, redemption, and payment of Series H bonds.

**§ 332.14 Reservations as to terms of offer.**

The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this offering of bonds, or of any amendments or supplements thereto.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 10.—Department Circular No. 653, Tenth Revision, offering of United States savings bonds, Series E**

DEPARTMENT OF THE TREASURY,  
*Washington, March 10, 1980.*

**SUMMARY:** This Tenth Revision of Department of the Treasury Circular No. 653, the offering circular for United States Savings Bonds of Series E, reflects (1) improvements in the investment yields of such bonds, (2) extensions granted for bonds not redeemed, and (3) changes in the terms necessitated by the termination of the offering. A notice in the Federal Register of December 31, 1979, announced that the sale of Series E savings bonds over-the-counter was terminated as of December 31, 1979, and that their issuance through payroll sales will terminate no later than June 30, 1980. They are being replaced by United States Savings Bonds of Series EE.

**EFFECTIVE DATE:** June 1, 1979.

**SUPPLEMENTAL INFORMATION:** This revision of the offering circular for Series E bonds effectuates two separate improvements in their investment yield. On May 10, 1979, the Secretary announced that the interest rate paid on these bonds would be increased, effective June 1, 1979, to 6.5 percent per annum, compounded semiannually. On December 12, 1979, he announced that Series E bonds would also receive an additional  $\frac{1}{2}$  of 1 percent bonus, if held for 11 years from the date of the first semiannual interest period that begins on or after January 1, 1980. Tables of redemption values and investment yields reflecting the improvements have been made a part of the circular.

The revision provides that the improvements in yield will be applied as follows:

**Interest Rate Increase To 6.5 Percent**

(1) Series E bonds bearing issue dates on or after June 1, 1979, will provide an investment yield of 6.5 percent, compounded semiannually, if held to original maturity, i.e., five years from issue date. The increase will be included as part of the redemption value of the bond as a one-time bonus at original maturity. If a bond is redeemed before original maturity, the yield will be less than 6.5 percent.

(2) Series E bonds bearing issue dates from December 1, 1974, through May 1, 1979, will reach original maturity from December 1, 1979, through May 1, 1984, five years after their respective issue dates. The  $\frac{1}{2}$  of 1 percent increase will apply to the remaining period to original maturity, effective with the first semiannual interest accrual period that begins on or after June 1, 1979. It will be included as part of the

## APPENDIX

Summary of investment yields to maturity and extended maturity dates under regulations prescribed for Series H savings bonds with issue dates from June 1, 1952.\*

Issues	Term to maturity (years and months)	Yield <sup>1</sup> during maturity period					Yield <sup>1</sup> during extended maturity period (10 years)					Yield <sup>1</sup> during second extended maturity period (10 years)		
		1959	1965	1968	1969	1970	1973	1979	1965	1968	1969	1970	1973	1979
5/52-3/54	9-8	3.00	+50						3.75e	+40	+10b	5.00	+50e	5.50e
8/54-9/54	9-8	3.00	+50						3.75e	+40	+10b	5.00	+50e	6.00e
10/54-9/55	9-8	3.00	+50						3.75e	+40	+10b	5.00	+50e	6.00e
10/55-3/56	9-8	3.00	+50						3.75e	+40	+10b	5.00	+50e	6.00e
4/56-11/56	9-8	3.00	+50						4.15e		+10b	5.00	+50e	6.00e
12/56-1/57	9-8	3.00	+50						4.15e		+10b	5.00	+50e	6.00e
2/57-5/58	10-0	3.25	+40						4.25b			5.00	+50e	6.00e
5/58-5/59	10-0	3.25	+40						5.00e			+50e	+50e	6.50e <sup>2</sup>
5/59-11/59	10-0	3.75							5.00e			+50e	+50e	6.50e <sup>2</sup>
12/59-5/60	10-0	3.75							5.50e			+50e	+50e	6.50e <sup>2</sup>
6/60-11/60	11-0	3.75							5.50e			+50e	+50e	6.50e <sup>2</sup>
12/60-12/61	10-0	3.75							5.50e			+50e	+50e	6.50e <sup>2</sup>
1/62-11/63	10-0	3.75							5.50e			+50e	+50e	6.50e <sup>2</sup>
12/63-5/64	10-0	3.75							6.00e			+50e	+50e	6.50e <sup>2</sup>
6/64-5/65	10-0	3.75							6.00e			+50e	+50e	6.50e <sup>2</sup>
6/65-11/65	10-0	3.75							6.00e			+50e	+50e	6.50e <sup>2</sup>
12/65-5/68	10-0	4.15							6.00e			+50e	+50e	6.50e <sup>2</sup>
6/68-5/69	10-0	4.25b							6.00e			+50e	+50e	6.50e <sup>2</sup>
6/69-11/69	10-0	5.00							6.50e			+50e	+50e	6.50e <sup>2</sup>
12/69-5/70	10-0	5.00							6.50e <sup>2</sup>			+50e	+50e	6.50e <sup>2</sup>
6/70-11/73	10-0	5.50							6.50e <sup>2</sup>			+50e	+50e	6.50e <sup>2</sup>
12/73-5/79	10-0	6.00							6.50e <sup>2</sup>			+50e	+50e	6.50e <sup>2</sup>
6/79-12/79	10-0	6.50							6.50e <sup>2</sup>					6.50e <sup>2</sup>

\* All yields are in terms of percent per annum, compounded semiannually. The first figure in each maturity period is the overall yield for that period at time of entry into period. Interest payments are on a graduated basis unless otherwise indicated, the full rate being received only if held to the end of the period (lesser rate if redeemed earlier). An "e" indicates payments on an approximately level basis. A "b" indicates increased interest on a bonus basis, that is, the full rate is received only if the bond is held to the end of the period (no increase if redeemed earlier). Rate increases within periods took effect at the beginning of the first full half-year interest period starting on or after the effective date as follows:

1959 — graduated improvements in rate to next maturity beginning June 1, 1959.

1965 — graduated improvement in rate to next maturity beginning Dec. 1, 1965.

1968 — bonus improvement in rate to next maturity beginning June 1, 1968.

1969 — maximum rate to next maturity beginning June 1, 1969.

1970 — level and bonus improvements in rate to next maturity beginning June 1, 1970. In the case of .50b the increase is spread over the second 5 years of maturity period.

1973 — level improvement in rate to next maturity beginning Dec. 1, 1973.

1979 — level improvement in rate to next maturity beginning June 1, 1979.

\* Yield does not apply if prevailing rate for Series H bonds at time extension begins is different from 6.50 percent.

\* The purpose of this table is to summarize the history of yields on Series H savings bonds. Because of the graduated nature of these yields this table does not contain sufficient detail for the calculation of individual checks.

redemption value of the bond as a one-time bonus at original maturity. The bond will not receive the increase if it is redeemed earlier.

(3) Series E bonds bearing issue dates from May 1, 1941, through November 1, 1974, will receive the  $\frac{1}{2}$  of 1 percent increase in yield effective with the first semiannual interest accrual period that begins on or after June 1, 1979. All of these bonds had entered an extended maturity period prior to December 1, 1979.

### 11-Year Bonus

Series E bonds that have not reached final maturity will also receive a one-time bonus of  $\frac{1}{2}$  of 1 percent, compounded semiannually, if they are held for 11 years from the first semiannual interest period that begins on or after January 1, 1980. The bonus will be added to the redemption value of outstanding bonds as of the first semiannual interest period that begins on or after January 1, 1991. A bond that is redeemed or reaches final maturity prior to completion of the 11-year period will receive the benefit of the 6.5 percent rate described above, but will not receive the additional bonus of  $\frac{1}{2}$  of 1 percent.

Other changes incorporated in the revision include the following:

*Termination of offering.* Section 316.1 provides that the offering of Series E bonds will terminate on December 31, 1979, except for bonds purchased through payroll savings plans, in which case the offering will terminate no later than June 30, 1980. This additional period for payroll savings plans is provided to allow employers operating such plans adequate time to convert their systems to the new Series EE bonds which were placed on sale as of January 1, 1980.

*Extended maturities.* Section 316.8, relating to the extended maturity periods granted to Series E bonds, is being revised. The term "extended maturity period" refers to one or more 10-year periods during which outstanding Series E bonds continue to accrue interest after the end of their original maturity period. In accordance with the Secretary's announcement of January 10, 1979, Series E bonds bearing issue dates of May 1, 1941, through April 1, 1952, will not be extended again. This group of bonds will thus reach final maturity exactly 40 years from their respective issue dates and will cease to earn interest at that time. All Series E bonds issued after April 1, 1952, are being granted an additional 10-year extension.

*Miscellaneous.* Several minor changes are being made to the offering to update addresses being used in connection with Series E bond transactions.

\* \* \* \* \*

Accordingly, Department of the Treasury Circular No. 653, Ninth Revision, dated April 23, 1974, as amended and supplemented, including the tables incorporated therein (31 CFR, Part 316), is hereby revised and amended and reissued as Department of the Treasury Circular No. 653, Tenth Revision, effective as of June 1, 1979.

This revision is effected under authority of Section 22 of the Second Liberty Bond Act, as amended (49 Stat. 21, as amended; 31 U.S.C. 757c) and 5 U.S.C. 301. Since this revision involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures thereon are unnecessary.

## PART 316—OFFERING OF UNITED STATES SAVINGS BONDS, SERIES E

### § 316.1 Offering of bonds.

The Secretary of the Treasury hereby offers for sale to the people of the United States, United States Savings Bonds of Series E, hereinafter generally referred to as "Series E bonds" or "bonds". This offer, containing revised terms effective as of June 1, 1979, will terminate as of December 31, 1979, except that, as to bonds purchased under payroll savings plans and employee plans, the offer will terminate no later than June 30, 1980.

### § 316.2 Description of bonds.

(a) *General.* Series E bonds bear a facsimile of the signature of the Secretary of the Treasury and of the Seal of the Department of the Treasury. They are issued only in registered form and are nontransferable.



(b) *Denominations and prices.* Series E bonds are issued on a discount basis.

The denominations and issue prices are:

Denomination:	Issue price
\$25.....	18.75
\$50.....	37.50
\$75.....	56.25
\$100.....	75.00
\$200.....	150.00
\$500.....	375.00
\$1,000.....	750.00
\$10,000.....	7,500.00
\$100,000 <sup>1</sup> .....	75,000.00

<sup>1</sup> The \$100,000 denomination was available only for purchase by trustees of employees' savings and savings and vacation plans (see Sec. 316.5(b)).

(c) *Inscription and issue.* At the time of issue the issuing agent will (1) inscribe on the face of each bond the name, social security number<sup>2</sup> and address of the owner, and the name of the beneficiary, if any, or the name, social security number and address of the first-named coowner and the name of the other coowner, (2) enter the issue date in the upper right-hand portion of the bond, and (3) imprint the agent's dating stamp in the lower right-hand portion to show the date the bond is actually inscribed. A bond shall be valid only if an authorized issuing agent receives payment therefor and duly inscribes, dates and stamps it.

(d) *Term.* A Series E bond shall be dated as of the first day of the month in which payment of the purchase price is received by an agent authorized to issue the bonds. This date is the issue date and the bond will mature and be payable at the maturity value, as shown in Table 174 hereof, 5 years from the issue date. The bond may not be called for redemption by the Secretary of the Treasury prior to maturity or the end of any extended maturity period (see § 316.8 (a) (1)). The bond may be redeemed at the owner's option at any time after 2 months from issue date at fixed redemption values.

(e) *Investment yield (interest).* —(1) *General.* The investment yield (interest) on a Series E bond will be approximately 6.5 percent per annum, compounded semiannually, if the bond is held to maturity, but the yield will be less if the bond is redeemed prior thereto. Beginning in the third month from such issue date, a bond will increase in redemption value on the first day of each month up to and including the thirtieth month from issue date so as to provide for such period an investment yield of no less than 4 percent per annum, compounded semiannually. Thereafter, its redemption value will increase at the beginning of each successive half-year period. The interest will be paid as part of the redemption value. See Table 174.

(2) *Additional bonus.* A bonus of  $\frac{1}{2}$  of 1 percent, compounded semiannually, will be added to the redemption value of any outstanding and unmatured Series E bond for the 11-year period commencing with the first semiannual interest accrual period beginning on or after January 1, 1980, but only if the bond is held to the end of such 11-year period.

### § 316.3 Governing regulations.

Series E bonds are subject to the regulations of the Department of the Treasury, now or hereafter prescribed, governing United States Saving Bonds of Series A, B, C, D, E, F, G, H, J and K, contained in Department of the Treasury Circular No. 530, current revision (31 CFR, Part 315).<sup>3</sup>

### § 316.4 Registration.

(a) *General.* Generally, only residents of the United States, its territories and possessions, the Commonwealth of Puerto Rico, and citizens of the United States temporarily residing abroad are eligible to be named as owners of Series E bonds. The bonds may be registered in the names of natural persons in their own right, as provided in paragraph (b) of this section, and in the names and titles or capacities of fiduciaries

<sup>2</sup> If the bond is being purchased as a gift or award and the owner's social security number is *not known*, the purchaser's social security number or employer identification number must be furnished. In this event, the issuing agent will inscribe the word "GIFT" and the purchaser's number on the bond.

<sup>3</sup> Copies may be obtained from any Federal Reserve Bank or Branch, from the Bureau of the Public Debt, Washington, D.C. 20226, or the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101.

and organizations, as provided in paragraph (c) of this section. Full information regarding authorized forms of registration and restrictions with respect thereto are found in the governing regulations.

(b) *Natural persons in their own right.* The bonds may be registered in the names of natural persons (whether adults or minors) in their own right, in single ownership, coownership, and beneficiary forms.

(c) *Others.* The bonds may be registered in single ownership form in the names of fiduciaries and private and public organizations, as follows:

(1) *Fiduciaries.* In the names of and showing the titles or capacities of any persons or organizations, public or private, as fiduciaries (including trustees, legal guardians or similar representatives, and certain custodians), but not where the fiduciary would hold the bonds merely or principally as security for the performance of a duty, obligation or service.

(2) *Private and public organizations.* In the names of private or public organizations (including private corporations, partnerships, and unincorporated associations, and States, counties, public corporations, and other public bodies) in their own right, but not in the names of commercial banks.<sup>4</sup>

### § 316.5 Limitation on holdings.

The amount of Series E bonds originally issued during any one calendar year that may be held by any one person, at any one time, computed in accordance with the governing regulations, is limited as follows:

(a) *General limitation.* \$10,000 (face amount) for any one calendar year.

(b) *Special limitation for employees' savings plans.* \$2,000 (face amount) multiplied by the highest number of participants in any employees' savings plan, as defined in paragraph (b) (1) of this section, at any time during the year in which the bonds are issued.<sup>5</sup>

(1) *Definition of plan and conditions of eligibility.* (i) The employees' savings plan must have been established by the employer for the exclusive and irrevocable benefit of employees or their beneficiaries, afford employees the means of making regular savings from their wages through payroll deduction, and provide for employer contributions to be added to such savings.

(ii) The entire assets thereof must be credited to the individual accounts of participating employees and the assets so credited may be distributed only to them or their beneficiaries, except as otherwise provided herein.

(iii) Series E bonds may be purchased only with assets credited to the accounts of participating employees and only if the amount taken from any account at any time for that purpose is equal to the purchase price of a bond or bonds in an authorized denomination or denominations, and shares therein are credited to the accounts of the individuals from which the purchase price thereof was derived, in amount corresponding with their shares. For example, if \$37.50 credited to the account of John Jones is commingled with funds credited to the accounts of other employees to make a total of \$7,500, with which a Series E bond in the denomination of \$10,000 (face amount) is purchased in December 1978 and registered in the name and title of the trustee, the plan must provide, in effect, that John Jones' account shall be credited to show that he is the owner of a Series E bond in the denomination of \$50 (face amount) bearing issue date of December 1, 1978.

(iv) Each participating employee shall have an irrevocable right at any time to demand and receive from the trustee all assets credited to his or her account or the value thereof, if he or she so prefers, without regard to any condition other than the loss or suspension of the privilege of participating further in the plan. However, a plan will not be deemed to be inconsistent herewith if it limits or modifies the exercise of any such right by providing that the employer's contribution does not vest absolutely until the employee shall have made contributions under the plan in each of not more

<sup>4</sup> For this purpose, commercial banks (as defined in Sec. 315.7, Department of the Treasury Circular No. 530, current revision) are those accepting demand deposits.

<sup>5</sup> Savings and vacation plans may be eligible for this special limitation. Questions concerning eligibility of such plans should be addressed to the Bureau of the Public Debt, Washington, D.C. 20226, or the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101.

than 60 calendar months succeeding the month for which the employer's contribution is made.

(v) Upon the death of an employee, his or her beneficiary shall have the absolute and unconditional right to demand and receive from the trustee all assets credited to the account of the employee, or the value thereof, if he or she so prefers.

(vi) When settlement is made with an employee or his or her beneficiary with respect to any bond registered in the name and title of the trustee in which the employee has a share (see paragraphs (b) (1) (ii) and (iii) of this section), the bond must be submitted for redemption or reissue to the extent of such share. If an employee or his or her beneficiary is to receive distribution in kind, bonds bearing the same issue dates as those credited to the employee's account will be reissued in the name of the distributee to the extent to which he or she is entitled, in any authorized form of registration, upon the request and certification of the trustee in accordance with the governing regulations.

(2) *Definitions of terms used in this subsection—related provisions.* (i) The term "savings plan" includes any regulations issued under the plan with regard to Series E bonds. A trustee desiring to purchase bonds in excess of the general limitation in any calendar year should submit to the Federal Reserve Bank of the district, a copy of (a) the plan, (b) any such regulations, and (c) the trust agreement, all certified to be true copies, in order to establish eligibility.

(ii) The term "assets" means all funds, including the employees' contributions and employer's contributions and assets purchased therewith as well as accretions thereto, such as dividends on stock, the increment in value on bonds and all other income; but, notwithstanding any other provision of this subsection, the right to demand and receive "all assets" credited to the account of an employee shall not be construed to require the distribution of assets in kind when it would not be possible or practicable to make such distribution; for example, Series E bonds may not be reissued in unauthorized denominations, and fractional shares of stock are not readily distributable in kind.

(iii) The term "beneficiary" means the person or persons, if any, designated by the employee in accordance with the terms of the plan to receive the benefits of the trust upon his or her death of the estate of the employee, and the term "distributee" means the employee or his or her beneficiary.

### § 316.6 Purchase of bonds.

Series E bonds may be purchased, as follows:

(a) *Over-the-counter for cash.* —(1) *Bonds registered in names of natural persons in their own right only.* At such incorporated banks, trust companies, and other agencies as have been duly qualified as issuing agents.

(2) *Bonds registered in names of trustees of employees' savings plans.* At such incorporated bank, trust company, or other agency, duly qualified as an issuing agent, provided the agent is trustee of an approved employees' savings plan eligible for the special limitation in § 316.5(b) and prior approval to issue the bonds is obtained from the Federal Reserve Bank of the agent's district.

(3) *Bonds registered in all authorized forms.* At Federal Reserve Banks and Branches and at the Department of the Treasury, Washington, D.C. 20226.

(b) *On mail order.* By mail upon application to any Federal Reserve Bank or Branch or to the Department of the Treasury, accompanied by a remittance to cover the issue price. Any form of exchange, including personal checks, will be accepted subject to collection. Checks or other forms of exchange should be drawn to the order of the Federal Reserve Bank or the United States Treasury, as the case may be. Checks payable by endorsement are not acceptable. Any depository qualified pursuant to the provisions of Department of the Treasury Circular No. 92, current revision (31 CFR, Part 203), will be permitted to make payment by credit for bonds applied for on behalf of its customers up to any amount for which it shall be qualified in excess of existing deposits, when so notified by the Federal Reserve Bank of its district.

(c) *Savings stamps.* The sale of United States Savings Stamps was terminated effective June 30, 1970. However, outstanding stamps affixed in fully or partially completed albums may be used to purchase Series E bonds at banks or other financial



institutions authorized to issue such bonds. Stamps may also be redeemed for cash at post offices.

### § 316.7 Delivery of bonds.

Issuing agents are authorized to deliver Series E bonds either over-the-counter in person, or by mail at the risk and expense of the United States, to the address given by the purchaser, but only within the United States, its territories and possessions, and the Commonwealth of Puerto Rico. No mail deliveries elsewhere will be made. If purchased by citizens of the United States temporarily residing abroad, the bonds will be delivered at such address in the United States as the purchaser directs.

### § 316.8 Extended terms and improved yields for outstanding bonds.

(a) *Extended maturity periods.* —(1) *General.* The terms “extended maturity period”, “second extended maturity period”, and “third extended maturity period”, when used herein, refer to 10-year intervals after the original maturity dates during which owners may retain their bonds and continue to earn interest on the maturity values or the extended maturity values.<sup>6</sup> No special action is required of owners desiring to take advantage of any extensions heretofore or herein granted.<sup>7</sup>

(2) *Bonds with issue dates from May 1, 1941, through April 1, 1952.* Series E bonds with issue dates from May 1, 1941, through April 1, 1952, will reach final maturity 40 years from their respective issue dates.

(3) *Bonds with issue dates from May 1, 1952, through November 1, 1965.* Owners of Series E bonds with issue dates from May 1, 1952, through November 1, 1965, may retain their bonds for a third extended maturity period of 10 years.

(4) *Bonds with issue dates from December 1, 1965, through June 1, 1980.* Owners of Series E bonds with issue dates from December 1, 1965, through June 1, 1980, may retain their bonds for a second extended maturity period of 10 years.

(b) *Improved yields<sup>8</sup> —Outstanding bonds.* The investment yield on all outstanding Series E bonds is hereby increased as follows:

(1) *Bonds reaching original maturity on or after December 1, 1979.* By approximately  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, to original maturity, on or after December 1, 1979, but only if the bonds are held to their respective maturity dates. The increase will be effective with the first interest accrual period starting on or after June 1, 1979.

(2) *Bonds which entered an extended maturity period prior to December 1, 1979.* By approximately  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, for the remaining period to their next maturity dates. The increase will be effective with the first interest accrual period starting on or after June 1, 1979.

(3) *Future extensions.* The investment yield for any future authorized extensions, other than as set forth in paragraphs b (1) or (2) of this section, will be at the rate of 6.5 percent per annum, compounded semiannually, unless such rate is changed prior to the commencement of the future extension period.

(4) *11-year bonus.* In addition to the improved yields specified above, a bonus of  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, will be paid for the 11-year period from the first semiannual interest period beginning on or after January 1, 1980, to the first semiannual interest period beginning on or after January 1, 1991, on all bonds which have not been redeemed or reached final maturity prior to completion of the 11-year period. Payment of the bonus will be made as part of the redemption value.

### § 316.9 Taxation.

(a) *General.* For the purpose of determining taxes and tax exemptions, the increment in value represented by the difference between the price paid for Series E bonds and the redemption value received therefor shall be considered as interest. Such interest is subject to all taxes imposed under the Internal Revenue Code of 1954. The bonds are

<sup>6</sup> The redemption value of any bond at the original and each extended maturity date is the base, in each instance, upon which interest will accrue during the period following.

<sup>7</sup> The tables incorporated herein, arranged according to issue dates, show current redemption values and investment yields (Not included in this exhibit but may be found in the Federal Register, Mar. 10, 1980.)

<sup>8</sup> See Appendix for summary of investment yields to the original and each extended maturity date under regulations heretofore and herein prescribed.

subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but are exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority.

(b) *Federal income tax on bonds.* An owner of Series E bonds who is a cash basis taxpayer may use either of two methods of reporting the increase in the redemption value of the bonds for Federal income tax purposes as follows:

(1) Defer reporting the increase to the year of final maturity, actual redemption, or other disposition, whichever is earlier; or

(2) Elect to report the increases each year as they accrue, in which case the election will apply to all Series E bonds then owned and to those thereafter acquired, as well as to any other similar obligations sold on a discount basis.

If the method in paragraph (b)(1) of this section is used, the taxpayer may change to the method in paragraph (b)(2) of this section without obtaining permission from the Internal Revenue Service. However, once the election to use the method in paragraph (b)(2) of this section is made, the taxpayer may not change the method of reporting unless he or she obtains permission to do so from the Internal Revenue Service. For further information on Federal taxes, consult the Service Center Director, or District Director, of the taxpayer's district, or the Internal Revenue Service, Washington, D.C. 20224.

#### **§ 316.10 Payment or redemption.**

(a) *General.* A Series E bond may be redeemed in accordance with its terms at the appropriate redemption value shown in the applicable table hereof. The redemption values of bonds in the denomination of "\$100,000" are not shown in the tables. However, the redemption value of a bond in that denomination will be equal to the total redemption values of ten \$10,000 bonds bearing the same issue dates. A bond in a denomination higher than \$25 (face amount) may be redeemed in part but only in the amount of an authorized denomination or multiple thereof.

(b) *Federal Reserve Banks and Branches and United States Treasury.* Owners of Series E bonds may obtain payment upon presentation and surrender of the bonds to a Federal Reserve Bank or Branch or to the Department of the Treasury with the request for payment on the bonds duly executed and certified in accordance with the governing regulations.

(c) *Incorporated banks, trust companies and other financial institutions.* An individual (natural person) whose name is inscribed on a Series E bond either as owner or coowner in his or her own right may present such bond to any incorporated bank or trust company or other financial institution which is qualified as a paying agent under Department of the Treasury Circular No. 750, current revision (31 CFR, Part 321). If such bond is in order for payment by the paying agent, the owner or coowner, upon establishing his or her identity to the satisfaction of the agent and upon signing the request for payment and adding his or her home or business address, may receive payment of its current redemption value.

#### **§ 316.11 Reservation as to issue of bonds.**

The Secretary of the Treasury reserves the right to reject any application for Series E bonds, in whole or in part, and to refuse to issue or permit to be issued hereunder any such bonds in any case or any class or classes of cases if he deems such action to be in the public interest, and his action in any such respect shall be final.

#### **§ 316.12 Preservation of rights.**

Nothing contained herein shall limit or restrict rights which owners of Series E bonds heretofore issued have acquired under offers previously in force.

#### **§ 316.13 Fiscal agents.**

Federal Reserve Banks and Branches, as fiscal agents of the United States, are authorized to perform such services as may be requested of them by the Secretary of

\* See footnote 1 to See 316.2

the Treasury in connection with the issue, delivery, redemption, and payment of Series E bonds.

**§ 316.14 Reservations as to terms of offer.**

The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this offering of bonds, or of any amendments or supplements thereto.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*



## APPENDIX

Summary of investment yields to maturity and extended maturity dates under regulations prescribed for Series E savings bonds with issue dates from May 1, 1941.\*

Issues	Terms to maturity (years and months)	Yield <sup>1</sup> during maturity period					Yield <sup>1</sup> during extended maturity period (10 years)					Yield <sup>1</sup> during second extended maturity period (10 years)					Yield <sup>1</sup> during third (and final) extended maturity period (10 years)				
		1959	1965	1968	1969	1970	1973	1979	1959	1965	1968	1969	1970	1973	1979	1965	1968	1969	1970	1973	1979
5/41-4/42	10-0	2.90						2.90	+ .60						3.75e	+ .40	+ .10b	5.00	+ .50e	5.50e	+ .50e
5/42-11/41	10-0	2.90						3.00e	+ .50						3.75e	+ .40	+ .10b	5.00	+ .50e	5.50e	+ .50e
12/43-5/44	10-0	2.90						3.00e	+ .50						3.75e	+ .40	+ .10b	5.00	+ .50e	6.00e	+ .50e
6/44-11/45	10-0	2.90						3.00e	+ .50						3.75e	+ .40	+ .10b	5.00	+ .50e	6.00e	+ .50e
12/45-5/48	10-0	2.90						3.00e	+ .50						4.15e		+ .10b	5.00	+ .50e	6.00e	+ .50e
6/48-5/49	10-0	2.90						3.00e	+ .50						4.25b			5.00	+ .50e	6.00e	+ .50e
6/49-11/49	10-0	2.90						3.75		+ .40	+ .10b				5.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/49-5/50	10-0	2.90	+ .60					3.75		+ .40	+ .10b	5.00			5.50e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/50-11/50	10-0	2.90	+ .60					3.75		+ .40	+ .10b	5.00	+ .50e		5.50e			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/50	10-0	2.90	+ .60					3.75		+ .40	+ .10b	5.00	+ .50e		5.50e			+ .50e	+ .50e	6.50e <sup>a</sup>	
1/51-4/52	10-0	2.90	+ .60					3.75		+ .40	+ .10b	5.00	+ .50e		5.50e			+ .50e	+ .50e	6.50e <sup>a</sup>	
5/52-3/54	9-8	3.00	+ .50					3.75		+ .40	+ .10b	5.00	+ .50e		6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
4/54-9/54	9-8	3.00	+ .50					3.75		+ .40	+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
10/54-5/55	9-8	3.00	+ .50					3.75		+ .40	+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/55-3/56	9-8	3.00	+ .50					3.75		+ .40	+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
4/56-11/56	9-8	3.00	+ .50					4.15e			+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/56-1/57	9-8	3.00	+ .50	+ .40				4.15e			+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
2/57-5/57	8-11	3.25	+ .50					4.15e			+ .10b	5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/57-5/59	8-11	3.25	+ .50					4.15e		+ .40		5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/59-5/60	7-9	3.75		+ .40				4.15e		+ .40		5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/60-5/61	7-9	3.75		+ .40				4.25b				5.00	+ .50e	+ .50e	6.00e			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/61-8/61	7-9	3.75		+ .40	+ .10b			4.25b				5.00	+ .50e	+ .50e	6.50e			+ .50e	+ .50e	6.50e <sup>a</sup>	
9/61-2/62	7-9	3.75		+ .40	+ .10b			5.00e				5.00e	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
3/62-8/62	7-9	3.75		+ .40	+ .10b			5.00e				5.00e	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
9/62-3/63	7-9	3.75		+ .40	+ .10b	5.00		5.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
4/63-5/63	7-9	3.75		+ .40	+ .10b	5.00		5.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/63-11/65	7-9	3.75		+ .40	+ .10b	5.00		5.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/65-11/66	7-0	4.15						5.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/66-5/67	7-0	4.15						5.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/67-5/68	7-0	4.15						6.00e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/68-5/69	7-0	4.25b						6.00e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/69-5/70	5-10	5.00						6.00e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/70-11/73	5-10	5.00b						6.00e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/73-5/74	5-0	6.00						6.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/74-11/74	5-0	6.00						6.50e				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
12/74-12/75	5-0	6.00						6.50e <sup>a</sup>				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
1/76-5/79	5-0	6.00						6.50e <sup>a</sup>				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	
6/79-6/80	5-0	6.50						6.50e <sup>a</sup>				5.00	+ .50e	+ .50e	6.50e <sup>a</sup>			+ .50e	+ .50e	6.50e <sup>a</sup>	

<sup>1</sup> All yields are in terms of percent per annum, compounded semiannually. The first figure in each maturity period is the overall yield for that period at time of entry into period. Crediting of accruals is on a graduated basis unless otherwise indicated, the full rate being credited only upon holding to end of period (lesser credit if redeemed earlier). An "e" indicates accrual on an approximately level basis. A "b" indicates increased accrual on a bonus basis; that is, full rate is credited only if bond is held to end of period (no increase if redeemed earlier). Rate increases within periods took effect at beginning of first full half-year interest accrual period starting on or after effective date as follows:

1959 - graduated improvements in rate to next maturity beginning June 1, 1959.

1965 - graduated improvement in rate to next maturity beginning Dec. 1, 1965.

1968 - bonus improvement in rate to next maturity beginning June 1, 1968, which took effect as early as Mar. 1, 1968, in some cases, but did not apply to first accrual period if it was less than a half-year.

1969 - maximum rate to next maturity beginning June 1, 1969.

1970 - bonus and level improvements in rate to next maturity beginning June 1, 1970.

1973 - level improvement in rate to next maturity beginning Dec. 1, 1973.

1979 - bonus and level improvement in rate to next maturity beginning June 1, 1979.

<sup>2</sup> Yield does not apply if prevailing rate for Series E bonds being issued at time extension begins is different from 6.50 percent.

<sup>3</sup> Yield does not apply if prevailing rate for Series E bonds being issued at time extension is different from 6.50 percent. During this maturity period, bonds held until their first interest accrual date in 1991 will receive a bonus payment which will increase their yield from their first semiannual interest accrual date in 1980 to their first interest accrual date in 1991 by  $\frac{1}{2}$  of 1%.

• The purpose of this table is to summarize the history of yields on Series E savings bonds. Because of the graduated nature of these yields this table does not contain sufficient detail for the calculation of redemption values.

**Exhibit 11.—Department Circular No. 3-67, Revised, Third Amendment, offering of United States savings notes**

DEPARTMENT OF THE TREASURY,  
*Washington, March 10, 1980.*

**SUMMARY:** This amendment of the offering circular for United States Savings Notes, i.e., Department of the Treasury Circular, Public Debt Series No. 3-67, as revised (31 CFR, Part 342), is being issued to show the improvements in the investment yields of savings notes and to grant a second 10-year extended maturity period to outstanding savings notes of all issue dates.

**EFFECTIVE DATE:** June 1, 1979.

**SUPPLEMENTAL INFORMATION:** On May 10, 1979, the Secretary of the Treasury announced that the interest rate paid on United States Savings Notes would be increased for semiannual interest periods that begin on or after June 1, 1979, to 6.5 percent per annum, compounded semiannually. On December 12, 1979, it was announced that savings notes would also receive an additional bonus of  $\frac{1}{2}$  of 1 percent, compounded semiannually, if held for 11 years from the date of the first semiannual interest period that begins on or after January 1, 1980. This amendment of the offering circular for savings notes effectuates these increases and provides tables of redemption values and investment yields which reflect the higher rate.

As provided in the amendment, the rate increase from 6 to 6.5 percent for the remaining period to the next maturity date will be included in the redemption value of savings notes for semiannual interest periods that begin on or after June 1, 1979. The interest on savings notes, including the increase, is payable as part of the redemption value when the notes are redeemed.

As regards the additional bonus provision, outstanding savings notes will have their yield for the 11-year period from the date of their first semiannual interest period starting on or after January 1, 1980, improved by  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, as a one-time bonus at the end of the period. Notes which are redeemed prior to the end of this 11-year period will only accrue interest at the 6.5 percent rate specified above.

Finally, a minor change is being made to the offering to update the address used in connection with transactions.

This amendment is effected under authority of Section 22 of the Second Liberty Bond Act, as amended (49 Stat. 21, as amended; 31 U.S.C. 757c) and 5 U.S.C. 301. Since this amendment involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures thereon are unnecessary.

Accordingly, Department of the Treasury Circular, Public Debt Series No. 3-67, Revised, dated August 14, 1968, as amended and supplemented (31 CFR, Part 342), is hereby further amended by the deletion of §342.2a and Tables 1-8 and the addition of new § 342.2a and new Tables 1-14 and the amendment of footnote 4 to § 342.9, as follows:

\* \* \* \* \*

**§ 342.2a Extended terms and improved yields for outstanding notes.**

(a) *Extended maturity periods.* The terms "extended maturity period" and "second extended maturity period", when used herein, refer to the 10-year intervals after the original maturity dates during which owners may retain their savings notes and continue to earn interest on the maturity values or the extended maturity values.<sup>4</sup> No special action is required of owners desiring to take advantage of any extensions heretofore or herein granted.<sup>5</sup> All savings notes may be retained for two extended maturity periods.

(b) *Improved yields.* The investment yield on all savings notes that are in their first extended maturity period on June 1, 1979, is hereby increased to 6.5 percent per

<sup>4</sup> The redemption value of any note at the original and each extended maturity date is the base, in each instance, upon which interest will accrue during the period following.

<sup>5</sup> The tables incorporated herein, arranged according to issue dates, show current redemption values and investment yields. (Not included in this exhibit but may be found in the Federal Register, Mar. 10, 1980.)



annum, compounded semiannually, for the remainder of such period, beginning with the first interest accrual period starting on or after June 1, 1979. The yield for notes thereafter entering a second extended maturity period will also be at that rate unless such rate is changed prior to the time the second extension period begins. The tables of redemption values and investment yields published herein will not apply if at the time the extension period begins the rate is different from 6.5 percent per annum, compounded semiannually.

(c) *Bonus provision.* In addition to the improved yields specified above, a bonus of  $\frac{1}{2}$  of 1 percent per annum, compounded semiannually, for the 11 year period commencing with the first semiannual interest accrual period which begins on or after January 1, 1980, will be applied to all notes held to the end of such period.

\* \* \* \* \*

#### § 342.9 [Amended]

Footnote 4 to § 342.9 is redesignated as footnote 6 and is amended as follows:

\* \* \* \* \*

\* Copies may be obtained from any Federal Reserve Bank or Branch, or the Bureau of the Public Debt, Washington, D.C. 20226, or the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101.

\* \* \* \* \*

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

#### **Exhibit 12.—Notice of requirement that social security numbers be furnished by owners at time of redemption of United States savings bonds and savings notes**

DEPARTMENT OF THE TREASURY,  
*Washington, June 12, 1980.*

**SUMMARY:** This document authorizes paying agents to require any person presenting for payment savings bonds of Series E and EE and savings notes to place his or her social security number on one or more of the securities redeemed. The paying agent is directed to refuse payment if the number is not furnished.

**EFFECTIVE DATE:** July 1, 1980.

**SUPPLEMENTARY INFORMATION:** Section 315.91 of Department of the Treasury Circular No. 530, as revised (31 CFR, Part 315), provides that the Secretary of the Treasury may require "that appropriate social security numbers be furnished for \* \* \* payment of any savings bond."

Section 353.91 of Department of the Treasury Circular, Public Debt Series, No. 3-80 (31 CFR, Part 353), provides that the "Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may require \* \* \* such additional evidence as he may consider necessary or advisable \* \* \*."

Pursuant to the authority set forth above, financial institutions qualified as paying agents of savings bonds are directed to require that any person presenting bonds of Series E and EE, and savings notes for payment place his or her social security

account number on one or more of the securities redeemed. Paying agents are further directed to refuse payment in any case where the number has not been furnished.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 13.—Department Circular No. 750, Third Revision, regulations governing payments by banks and other financial institutions of United States savings bonds and United States savings notes**

DEPARTMENT OF THE TREASURY,  
*Washington, June 20, 1980.*

**SUMMARY:** Department of the Treasury Circular No. 750 (31 CFR, Part 321) contains the regulations governing financial institutions qualified to redeem United States Savings Bonds and United States Savings Notes. This Third Revision of the Circular is necessary because of changes in the Savings Bond Program involving (1) the introduction of Series EE savings bonds; (2) the introduction of a redemption-exchange offer for Series HH savings bonds; and (3) the withdrawal from sale of Series H savings bonds and the termination of the Series H exchange offer.

**EFFECTIVE DATE:** July 1, 1980.

**SUPPLEMENTARY INFORMATION:** Department of the Treasury Circular No. 750, Second Revision, authorized qualified paying agents to: (1) redeem Series A, B, C, D, and E savings bonds and savings notes presented for payment, and (2) to redeem eligible securities presented in exchange for Series H bonds.

Effective as of January 1, 1980, several changes were made to the Savings Bonds Program, including the introduction of new Series EE and HH bonds and a new Series HH exchange offering, concurrent with the termination of sale of Series E and H bonds and the withdrawal of the Series H exchange offering.

The Third Revision of Circular No. 750 provides for these Program changes by extending the payment authority of qualified agents to include eligible Series EE bonds, as well as the Series A-E bonds and savings notes. Additionally, qualified agents are authorized to redeem eligible Series EE and E bonds and savings notes in exchange for the new Series HH bonds.

All paying agents currently qualified are automatically requalified to redeem savings bonds and notes in accordance with the provisions of the Third Revision.

Department of the Treasury Circular No. 751, Second Revision, contained regulations regarding the manner of accounting for losses resulting from the erroneous redemption of savings bonds and notes. This material has now been incorporated, without substantive change, in the Third Revision of Circular No. 750, and Circular No. 751 is being rescinded.

Apart from the changes already mentioned, the Third Revision of Circular No. 750 does not differ substantially from the Second Revision. Where appropriate, there has been some reorganization of the contents and rewording for clarity. Differences between the two revisions are discussed in the following paragraphs.

### **General Information**

The definitions in Sec. 321.1 have been reordered and expanded.

### **Procedures for Qualification**

Subpart B has been retitled and contains the instructions regarding the manner in which eligible financial institutions may qualify and serve as paying agents. Although the material in the Third Revision has been reorganized and expanded, there are no substantive differences between it and the provisions of the Second Revision contained in Secs. 321.2, 321.3, 321.4 and 321.6. Paragraph (c) of Sec. 321.5 is new, but the reservation it expresses was implicit in the earlier revision.

### Scope of Authority

Sec. 321.6 is substantially the same as the previous Sec. 321.7 but includes reference to the regulations governing the new Series EE bonds. The prohibition against payment to a designated beneficiary was moved from this section to Sec. 321.9.

Sec. 321.7 deals with bonds and notes presented for cash redemption and contains information formerly in Sec. 321.8. It also extends the redemption authority of agents to Series EE bonds.

Sec. 321.8 replaces the previous Sec. 321.9 and authorizes the agents to redeem eligible bonds and notes presented in exchange for Series HH bonds under the provisions of Department of the Treasury Circular, Public Debt Series No. 2-80. This section also covers in more detail the requirements for redemption-exchange.

Sec. 321.9 lists the securities not eligible for payment by agents, replacing the previous Sec. 321.10. The current list has been updated to include Series EE bonds presented within six months after issue. It has also been expanded to identify more specifically such ineligible securities as those presented: by a beneficiary, by anyone acting under a power of attorney, or by a presenter whose social security number is not furnished.

Sec. 321.10 contains information regarding the responsibilities of agents to pay eligible securities and the restrictions against the collateralizing and discounting of securities. This material was formerly in the Memorandum of Instructions Issued in Conjunction with the Second Revision of the Circular.

### Payment and Transmittal

With some title changes and required updating, Secs. 321.11, 321.12, 321.13 and 321.14 of Subpart D contain material previously in Secs. 321.12, 321.13 and 321.14.

### Losses Resulting From Erroneous Payments

Subpart E is new. It contains material formerly in Sec. 321.15 of Circular No. 750, in the Memorandum of Instructions, and in Circular No. 751, Second Revision. Although the information has been reorganized, it contains no basic changes in the existing procedures or substantive rules for dealing with erroneous payments and losses resulting from such payments.

### Forwarding Items

Subpart F contains material previously in Sec. 321.11, without significant change.

### Miscellaneous

Sec. 321.23 provides information regarding fees formerly in Sec. 321.5. The new material states that details regarding the fee schedule will be published separately in the Federal Register.

Sec. 321.24 contains information regarding claims on account of lost securities, which was formerly in the Memorandum of Instructions.

### Appendix <sup>1</sup>

The Memorandum of Instructions Issued in Conjunction with Department Circular No. 750, Second Revision, is being replaced by an Appendix to the Third Revision. The Appendix supplements the provisions of Circular No. 750 and provides additional guidance to agents on the payment and processing of securities. The Appendix will be subject to amendment or revision from time to time by the Commissioner of the Public Debt to incorporate nonregulatory changes that affect the activities of paying agents under the provisions of the Circular and its Appendix.

Accordingly, Department of the Treasury Circular No. 751, Second Revision, dated October 25, 1968 (31 CFR, Part 322) is hereby revoked, and Department of the Treasury Circular No. 750, Second Revision, dated October 25, 1968 (31 CFR, Part

<sup>1</sup> Not included in this exhibit. Is in the Federal Register, June 20, 1980.



321) is hereby revised and reissued as Department of the Treasury Circular No. 750, Third Revision, effective July 1, 1980.

This revocation and revision are effected under authority of Section 22 of the Second Liberty Bond Act, as amended (49 Stat. 21, as amended; 31 U.S.C. 757c) and 5 U.S.C. 301. Since these actions involve the fiscal policy of the United States and do not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary.

31 CFR is amended as follows:

## PART 322 (REVOKED)

1. Part 322 is revoked.
2. Part 321 is revised to read as follows:

### PART 321—PAYMENTS BY BANKS AND OTHER FINANCIAL INSTITUTIONS OF UNITED STATES SAVINGS BONDS AND UNITED STATES SAVINGS NOTES (FREEDOM SHARES)

#### SUBPART A—GENERAL INFORMATION

##### § 321.0 Purpose.

The regulations in this Part govern the manner in which financial institutions may qualify and act as paying agents for the redemption of (a) United States Savings Bonds of Series A, B, C, D, E, and EE and United States Savings Notes (Freedom Shares) presented for cash payment; and (b) eligible Series E and EE savings bonds and savings notes presented for redemption in exchange for Series HH savings bonds under the provisions of Department of the Treasury Circular, Public Debt Series No. 2-80 (31 CFR, Part 352).

##### § 321.1 Definitions.

(a) "Cash payment" means payment in currency, by check or by credit to a checking, savings or share account.

(b) "Federal Reserve Bank" or "Bank" refers to the Federal Reserve Bank of the district in which a paying agent or applicant-organization is located and includes the Branch(es) of the Bank, where appropriate.

(c) "Owner" means an individual whose name is inscribed as owner or coowner in his or her own right on a bond or note.

(d) "Paying agent(s)" or "agent(s)" means (1) any eligible financial institution qualified under the provisions of this Circular, as originally issued, or any subsequent revision, to make payments of savings bonds and notes, and includes branches of such institutions located within the United States, its territories and possessions, and the Commonwealth of Puerto Rico; and (2) any banking facilities of such institutions established at military installations overseas, provided the offering of such redemption services has been authorized by the Department of the Treasury.

(e) "Presenter" means the individual requesting the redemption or redemption-exchange of securities.

(f) "Redemption" and "payment" are used interchangeably for payment of a bond or note in accordance with the terms of its offering and the regulations governing the security, including redemption-exchange.

(g) "Redemption-exchange" means the authorized redemption of eligible securities for the purpose of applying the proceeds in payment for other securities offered in exchange by the Treasury.

(h) "Savings bond(s)" or "bond(s)" means a United States Savings Bond of Series A, B, C, D, E, or EE.

(i) "Savings note(s)" or "note(s)" means a United States Savings Note (Freedom Share).

(j) "Security" or "securities" means a savings bond or savings note, as defined in (f) and (g) of this section.

## SUBPART B—PROCEDURES FOR QUALIFICATION

**§ 321.2 Eligible organizations.**

Organizations eligible to apply for qualification and to serve as paying agents are commercial banks, trust companies, savings banks, savings and loan associations, building and loan associations (including cooperative banks), credit unions, cash depositories, industrial banks, and similar financial institutions which (a) are incorporated under Federal law or the laws of a State, territory or possession of the United States, the District of Columbia, or the Commonwealth of Puerto Rico; (b) in the usual course of business accept, subject to withdrawal, funds for deposit or the purchase of shares; (c) are under the supervision of the banking department or equivalent authority of the jurisdiction in which incorporated; and (d) maintain regular offices for the transaction of their business.

**§ 321.3 Procedure for qualifying and serving as paying agent.**

(a) *Execution of application-agreement.* An eligible organization wishing to act as a paying agent shall obtain from, execute and file with a Federal Reserve Bank an application-agreement form. The terms of each application-agreement shall include the provisions prescribed by Sec. 202 of Executive Order No. 11246, entitled 'Equal Employment Opportunity' (3 CFR, Subchapter B, 42 U.S.C. 2000e note). For the purpose of these regulations, eligible institutions in Puerto Rico and the Virgin Islands shall make application to the Federal Reserve Bank of New York, and eligible institutions in Guam shall make application to the Federal Reserve Bank of San Francisco.

(b) *Qualification.* Each Federal Reserve Bank, as fiscal agent of the United States, is authorized to qualify any eligible institution located in its district which possesses adequate authority under its charter to act as paying agent. Upon approval of an application-agreement, the Federal Reserve Bank will issue a certificate of qualification to the organization. Such a certificate automatically qualifies the domestic branches of the organization to redeem securities.

(c) *Announcement of authority.* Upon receipt of a certificate of qualification from a Federal Reserve Bank, a financial institution may announce or advertise its authority to cash bonds and notes and process exchanges of Series E and EE bonds and notes for Series HH bonds.

(d) *Adverse action.* An organization will be notified by the Federal Reserve Bank in writing if its application-agreement to act as paying agent is not approved.

**§ 321.4 Paying agents previously qualified.**

Institutions qualified as paying agents under previous revisions of this Circular are authorized to continue to act in that capacity without requalification. By so acting, they shall be subject to the terms and conditions of their previously executed application-agreements and these regulations in the same manner and to the same extent as though they had requalified hereunder.

**§ 321.5 Termination of qualification.**

(a) *By the Treasury.* The Secretary of the Treasury or his delegate, the Commissioner of the Public Debt, may authorize a Federal Reserve Bank to terminate the qualification of any paying agent at any time, following prior written notice of such action to the agent.

(b) *At request of paying agent.* A Federal Reserve Bank will terminate the qualification of a paying agent upon its written request, provided the agent renders a final accounting for all paid bonds, and is found to have fully complied with the terms of its agreement and the applicable regulations and instructions.

(c) *Reservation.* Termination of the qualification as paying agent of any institution shall not prejudice the right of the Treasury to recover the amounts of any erroneous payments made by the institution subsequent to the termination.

## SUBPART C—SCOPE OF AUTHORITY

**§ 321.6 General.**

Savings bonds and savings notes are issued only in registered form, are not transferable, may not be hypothecated or used as collateral for a loan, and, except as otherwise specifically provided for in the governing regulations, are payable only to the owner or coowner named on the securities. The regulations governing Series EE and HH bonds are contained in Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR, Part 353), and those governing all other savings bonds, as well as savings notes, are contained in Department of the Treasury Circular No. 530, current revision (31 CFR, Part 315).

**§ 321.7 Authorized cash payments.**

(a) *General.* Subject to the terms and conditions appearing on the securities, the governing regulations, and the provisions of this Circular and any instructions issued in connection therewith, an agent may make payment of savings bonds of Series A, B, C, D, E, and EE and savings notes presented for cash redemption. Except as provided in (b) and (c) of this section, the securities must be presented for redemption by an individual whose name is inscribed on the securities as owner or coowner, and who is known to the agent or can establish his or her identity in accordance with Treasury instructions and guidelines. (See Sec. 321.12(b).)

(b) *Change of name by marriage.* If the name of the owner or coowner inscribed on the security has been changed by marriage and the agent knows or establishes that the presenter and the person whose name appears on the security are one and the same individual, the agent may pay the security in accordance with paragraph (a) of this section. The signature to the request for payment should show both names, for example, "Mary J. Smith, changed by marriage from Mary T. Jones".

(c) *Parent of a minor.* If the name of the owner inscribed on the security is that of a minor child who is not of sufficient competency and understanding to execute the request for payment and comprehend the nature of the act, payment may be made to either parent with whom the child resides or to whom custody has been granted, provided the form of registration does not indicate that a guardian or similar representative of the estate of the minor owner has been appointed or is otherwise legally qualified. The parent requesting payment must sign the request for payment in the form, for example, "John A. Jones, on behalf of John C. Jones", and place an endorsement in substantially the following form, which may be typed or imprinted, on the back of the security:

"I certify that I am the (father or mother) of John C. Jones and the person (with whom he resides) (to whom custody has been granted). He is — years of age and is not of sufficient competency and understanding to sign the request."

Payment under this paragraph may not be made to any person other than a father or mother.

**§ 321.8 Redemption-exchange of Series E and EE Savings Bonds and Savings Notes.**

(a) *General.* Subject to the provisions of Circular No. 2-80, the governing regulations, and the provisions of this Circular and its Appendix, an agent may make payment of eligible savings bonds of Series E and EE and savings notes presented for redemption in exchange for Series HH bonds. Securities eligible for exchange are (1) Series E bonds presented no later than one year after their final maturity dates; (2) Series EE bonds presented no earlier than six months after their issue dates; and (3) all savings notes.

(b) *Requirements for redemption-exchange.* Agents shall not accept and redeem eligible securities on exchange unless:

(1) The securities are accompanied by a completed exchange subscription form signed by the person requesting the exchange;

(2) The person requesting the exchange is (i) the owner named on the surrendered securities who is to be named as owner or first-named coowner on the Series HH bonds; (ii) the "principal coowner", as defined in Sec. 352.7(e)(2) of Circular No. 2-80,



who is to be named as owner or first-named coowner on the Series HH bonds; or (iii) either coowner, if the form of registration requested for the Series HH bonds is identical to that appearing on all of the surrendered securities; and

(3) The request for payment on each surrendered security is signed by the person requesting the exchange, unless the agent is authorized and elects to use the special endorsement procedure provided for in Department of the Treasury Circular No. 888, current revision (31 CFR, Part 330).

If the name of the presenter has been changed by marriage, the agent may process the transaction in accordance with the provisions of Sec. 321.7(b) of this Circular.

(c) *Completion of transaction.* The agent shall forward securities redeemed on exchange, the exchange subscription and full payment of the issue price of the Series HH bonds to the Federal Reserve Bank, which will complete the transaction by issuing the new bonds. (See Sec. 321.14.)

### § 321.9 Specific limitations on payment authority.

An agent is not authorized to pay a security for cash or on redemption-exchange:

(a) If it is a Series EE bond presented for payment prior to the end of six months from its issue date.

(b) If it is a savings bond of Series F, G, H, J, K, or HH.

(c) If the presenter is the designated beneficiary.

(d) If the presenter is acting under a power of attorney.

(e) If the agent does not know or cannot establish the identity of the presenter as the owner of the security, including the establishment of the identity of a parent requesting payment on behalf of a minor child, as provided in Sec. 321.7(c).

(f) If the presenter does not sign his or her name in ink as it is inscribed on the security and show a home or business address. (See also Sec. 321.7(b) and (c).)

(g) If the presenter's social security number is not shown in the inscription and he or she refuses to furnish the number.

(h) If the security bears a material irregularity, such as an illegible, incomplete or unauthorized inscription, issue date or issuing agent's validating stamp impression; or if any essential part of the security appears to have been altered or is mutilated or defaced in such a manner as to create doubt or arouse suspicion.

(i) If the security is registered in the name of a corporation, association, partnership, or other organization, or a guardian, administrator, trustee, or other fiduciary.

(j) If Treasury regulations require the submission of documentary evidence to support the redemption, as in the case of deceased owners, incompetents, or minors under legal guardianship, or the change of an owner's name other than by marriage.

(k) If the presenter is a minor who, in the opinion of the agent, is not of sufficient competency and understanding to execute the request for payment and comprehend the nature of the act.

(l) If it is known to the agent that the owner has been legally declared incompetent to manage his or her affairs.

(m) If partial redemption is requested.

### § 321.10 Responsibilities of paying agents.

(a) *Payment of securities.* A financial institution qualified as a paying agent is required to cash eligible savings bonds and savings notes for any presenter, whether or not a customer, during its regular business hours, in accordance with the provisions of this Circular and its Appendix, and the Treasury Identification Guide for Cashing United States Savings Bonds.

(b) *Restrictions.* A paying agent shall not advance money, or make loans on, or discount the redemption value of securities, nor in any manner assist others to do so. An agent shall not pay an owner the current value of a security and then defer presentation to the Treasury for the purpose of obtaining for its own profit an increased value.

## SUBPART D—PAYMENT AND TRANSMITTAL OF SECURITIES

**§ 321.11 Payment.**

(a) *Examination.* Before making payment of a security, the agent shall examine it to determine that it is eligible for redemption and is one the agent is authorized to pay under the provisions of this Circular.

(b) *Identification.* The agent shall determine that the individual presenting the security is the same person whose name is inscribed as owner or coowner, except as provided in Sec. 321.7(b) and (c). Unless the presenter is a person whose identity is well-known to the agent, or is an established customer, he or she should be asked to furnish satisfactory identification in accordance with the Treasury instructions and guidelines. At the time of payment, the agent should make a notation on the back of the security, or in its own records, specifying precisely what was relied on to establish the presenter's identity.

(c) *Execution of request.* The agent shall require that the request for payment on the back of each security be executed by the presenter in the presence of one of its officers or authorized employees, unless the agent is qualified under Circular No. 888, current revision, and elects to use the special endorsement procedure. If the request has already been executed when the security is presented, it should ordinarily be reexecuted.

(d) *Certification of request.* An agent is not required to complete the certification to the request for payment on securities it redeems.

**§ 321.12 Redemption value of securities.**

The redemption value of each security, which is based on the length of time it has been outstanding, is published in a redemption value table appended to the offering circular. The Bureau of the Public Debt provides each agent with booklets containing tables showing the redemption values of eligible securities during each month, that are to be used in paying the securities.

**§ 321.13 Cancellation of redeemed securities.**

An agent shall cancel each redeemed security by imprinting the word "PAID" on its face and entering the amount and date of the actual payment, and the name, location and code number assigned to the agent by the Federal Reserve Bank. The recordation of this data shall constitute a certification by the agent that the security was redeemed in accordance with the provisions of this Circular, that the identity of the presenter was duly established, and that the proceeds were paid to the presenter or remitted to a Federal Reserve Bank in payment for Series HH bonds.

**§ 321.14 Transmittal to and settlement by a Federal Reserve Bank.**

The paying agent shall forward securities redeemed for cash and on redemption-exchange, with covering transmittal letter forms, to the Federal Reserve Bank in accordance with the latter's instructions. Upon receipt of the securities, the Bank will make immediate settlement with the paying agent for the total amount paid, as reflected on the transmittal letter form. Such settlement shall be subject to adjustment if discrepancies are subsequently discovered. The Federal Reserve Bank will forward all redeemed securities to the Bureau of the Public Debt for audit.

## SUBPART E—LOSSES RESULTING FROM ERRONEOUS PAYMENTS

**§ 321.15 Statutory provisions.**

Under the governing statute, as amended (Title 31, United States Code, Sec. 757c(i)), an agency that redeems savings bonds and savings notes cannot be relieved of liability for a loss resulting from an erroneous payment unless the Secretary of the Treasury can make a determination that the loss resulted from no fault or negligence on the part of the agency.

**§ 321.16 Report of erroneous payment.**

If a paying agent discovers an erroneous payment of securities, it should immediately advise the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101. If the circumstances of the payment warrant such action, the agent should also notify the nearest office of the United States Secret Service.

**§ 321.17 Investigation of potential loss.**

(a) *Notice to agent.* When it determines that a potential loss has occurred because of the erroneous payment of securities, the Bureau of the Public Debt will promptly notify the paying agent in writing, identifying the securities and furnishing appropriate details and instructions. Notification may also be made through a personal visit from a Secret Service agent, rather than in writing.

(b) *Investigative procedure.* The Bureau of the Public Debt shall request the United States Secret Service to investigate potential losses and to assist in the recovery of improper payments. The paying agent, upon receipt of notification of an erroneous payment, shall make available to the Bureau of the Public Debt or its investigative agent all records and information pertaining to the redemption transaction in question, including the disposition of the redemption proceeds. If those proceeds were deposited in an account maintained by the agent, the information made available shall include the ultimate disposition of the redemption proceeds from the account.

(c) *Opportunity to present evidence.* The paying agent involved in any erroneous payment shall be given every opportunity to present the full facts relating to the payment, prior to a determination of final loss.

**§ 321.18 Determination of loss.**

Upon completion of the investigation, and after consideration of the results, the Bureau of the Public Debt shall advise the agency through which the payment occurred:

(a) That no final loss to the United States has occurred, and, accordingly, that it is relieved from liability for the payment, or that no claim for reimbursement shall be made unless and until a loss has been sustained; or

(b) That while a final loss to the United States has occurred, it is not required to make reimbursement therefor, as the Secretary of the Treasury, or the Commissioner of the Public Debt, as his delegate, has determined that such loss resulted from no fault or negligence on the part of such agency; or

(c) That a final loss to the United States has occurred, and that, as the Secretary of the Treasury, or the Commissioner of the Public Debt, as his delegate, has been unable to make an affirmative finding that such loss resulted from no fault or negligence on the part of such agency, reimbursement must be made promptly, except where credit for the payment had not previously been extended.

**§ 321.19 Certification of signatures.**

The regulations in this Subpart shall, to the extent appropriate, apply to losses resulting from payments made in reliance on certifications of signatures to any requests for payment of savings bonds and savings notes by an officer or designated employee of any financial institution authorized to certify such requests.

**§ 321.20 Applicability of provisions.**

The provisions of this Subpart shall apply to securities redeemed by any Federal Reserve Bank, as fiscal agent, or any Treasury office authorized to pay savings bonds and notes, as well as to qualified paying agents.

**§ 321.21 Replacement and recovery of losses.**

If a final loss has resulted from the redemption of a savings bond or savings note, and no reimbursement has been or will be made, the loss shall be subject to replacement out of the fund established by the Government Losses in Shipment Act, as amended.



## SUBPART F—FORWARDING ITEMS

**§ 321.22 Forwarding securities not payable by an agent.**

Any securities an agent is not authorized to pay under the provisions of this Circular should be forwarded for redemption, with the requests for payment properly certified, to a Federal Reserve Bank or to the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101. Any documentary evidence required to support the redemption should accompany the securities. If the securities are presented for redemption-exchange, they must also be accompanied by a completed exchange subscription and the cash difference, if any, due on the exchange. If an institution undertakes to forward unpaid securities at the request of and on behalf of the person entitled to payment, they must be transmitted separately from securities the institution has paid.

## SUBPART G—MISCELLANEOUS PROVISIONS

**§ 321.23 Paying agent fees and charges.**

(a) *Fees.* Paying agents receive a fee for each security redeemed. A schedule setting out the fees and the basis on which they are computed and paid is separately published in the Federal Register. Current information is available from a Federal Reserve Bank or the Bureau of the Public Debt.

(b) *Charges to owners.* Paying agents shall not make any charge whatever to owners of savings bonds and savings notes for redeeming securities under the provisions of this Circular.

**§ 321.24 Claims on account of lost securities.**

If a security paid by an agent is lost, stolen or destroyed while in the custody of the agent or while in transit to a Federal Reserve Bank, the Bureau of the Public Debt will consider an agent's claim for reimbursement of the amount paid on the missing security, provided it can be identified by serial number.

**§ 321.25 Role of Federal Reserve Banks.**

The Federal Reserve Banks, as fiscal agents of the United States, shall perform such services in connection with this Part as may be requested by the Secretary of the Treasury or his delegate, the Commissioner of the Public Debt. The Banks are authorized and directed to perform such duties, including the issuance of instructions and forms, as may be necessary to fulfill the purposes and requirements of these regulations.

**§ 321.26 Preservation of rights.**

Nothing contained in this Circular shall limit or restrict any existing rights which holders of savings bonds and savings notes may have acquired under the Circulars offering the securities for sale and the applicable regulations.

### § 321.27 Supplements, amendments, or revisions.

The Secretary of the Treasury may, at any time or from time to time, revise, supplement, amend or withdraw, in whole or in part, the provisions of this Circular.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

### Exhibit 14.—Department Circular No. 888, Fourth Revision, Regulations governing payment under special endorsement of United States savings bonds and United States savings notes

DEPARTMENT OF THE TREASURY,  
*Washington, June 20, 1980.*

**SUMMARY:** Department of the Treasury Circular No. 888 (31 CFR, Part 330) contains the regulations governing the payment of United States Savings Bonds and United States Savings Notes (Freedom Shares) under special endorsement. The Fourth Revision of this Circular is necessary because of changes in the Savings Bond Program involving (1) the introduction of Series EE bonds; (2) the introduction of a redemption-exchange offer for Series HH bonds; and (3) the withdrawal from sale of Series H bonds and the termination of the Series H exchange offer. The Fourth Revision also rescinds the authority of qualified agents to specially endorse and pay Series F, G, J, and K savings bonds under the provisions of the Third Revision.

**EFFECTIVE DATE:** July 1, 1980.

**SUPPLEMENTARY INFORMATION:** Department of the Treasury Circular No. 888, Third Revision, authorized qualified agents to use a special endorsement, in lieu of obtaining the owner's signature to the request for payment, for certain series of savings bonds and for savings notes. The special endorsement authority applied to savings bonds of Series A, B, C, D, E, F, G, J, and K, as well as notes. Qualified agents were also authorized to redeem for cash or in exchange for Series H bonds certain classes of specially endorsed securities.

The Fourth Revision of this Circular continues the authority of qualified agents to use the special endorsement procedures, but revises the various series of savings bonds that can be processed under the procedure. Securities now eligible for special endorsement are Series A, B, C, D, E, and EE savings bonds, as well as savings notes.

Specially endorsed securities which a qualified agent may redeem for cash or in exchange for Series HH bonds are restricted to those securities an agent is otherwise authorized to redeem under the provisions of Department of the Treasury Circular No. 750, Third Revision. These include (1) Series A, B, C, D, E, and EE savings bonds and notes presented for cash redemption by an individual named as owner or coowner, and (2) eligible Series E and EE bonds and savings notes presented for redemption-exchange by an individual named as owner or coowner.

All agents currently qualified to exercise the special endorsement authority are automatically requalified under the provisions of the Fourth Revision.

The Memorandum of Instructions Issed in Conjunction with Department Circular No. 888, Third Revision, is no longer considered necessary and is not being republished. Significant material in the Memorandum has been incorporated in the Fourth Revision.

Apart from the changes cited, the Fourth Revision does not differ substantially from the Third Revision. There have been some changes in organization and language for clarification. Differences between the two revisions are discussed in the paragraphs that follow.

The Purpose of the Circular, as stated in Sec. 330.0, has been revised. The restrictions relating to pledge, hypothecation, etc., previously contained in this section have been moved to Sec. 330.3(d).

A set of definitions of terms used in the Circular has been added as Sec. 330.1. Sec. 330.2 contains instructions regarding the qualification procedures, formerly in Sec. 330.1. The instructions have been expanded and rearranged.

Sec. 330.3 covers instructions formerly in Secs. 330.5 and 330.6, augmented by material formerly in paragraphs 6 and 7 of the Memorandum of Instructions. As indicated, paragraph (d) contains the restrictions previously in Sec. 330.0.

Sec. 330.4 was formerly Sec. 330.3.

Sec. 330.5 replaces previous Sec. 330.4. Paragraph (a) contains new material regarding the signature on the exchange subscription, Form PD 3253. Paragraphs (b) and (c) were formerly in paragraph 5 of the Memorandum.

Sec. 330.6(a) contains the general authority of agents to specially endorse securities and replaces Sec. 330.2. Paragraph (b) has material previously in Sec. 330.2 and paragraph 4 of the Memorandum. Paragraph (c) has material formerly in paragraph 8 of the Memorandum.

The material in Sec. 330.7 was formerly in Sec. 330.7(a)(1) and (3) and paragraph 8 of the Memorandum. It has been restated.

Sec. 330.8 contains material formerly in Sec. 330.7(b), also restated.

Secs. 330.9, 330.10 and 330.11 replace Secs. 330.8, 330.9 and 330.11, without substantial change. Old Sec. 330.10 has been dropped as unnecessary.

Accordingly, Department of the Treasury Circular No. 888, Third Revision, dated December 10, 1968 (31 CFR, Part 330) is hereby revised and reissued as Department Circular No. 888, Fourth Revision, effective July 1, 1980.

Since this revision involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary.

Part 330 of title 31 CFR is revised to read as follows:

## PART 330—REGULATIONS GOVERNING PAYMENT UNDER SPECIAL ENDORSEMENT OF UNITED STATES SAVINGS BONDS AND UNITED STATES SAVINGS NOTES (FREEDOM SHARES)

### § 330.0 Purpose.

The regulations in this Part establish a procedure under which qualified paying agents may specially endorse United States Savings Bonds of certain series and United States Savings Notes (Freedom Shares), and either redeem the securities so endorsed, or forward them to a Federal Reserve Bank for redemption, with or without the owner's signature to the requests for payment.

### § 330.1 Definition of terms.

As used in this Circular:

(a) "Federal Reserve Bank" or "Bank" refers to the Federal Reserve Bank of the district in which a paying agent is located, and includes the Branch(es) of the Bank, where appropriate.

(b) "Owner(s)" means the person named as registered owner or coowner on a bond or note and applies generally to individuals. For the purposes of special endorsement, but not payment, by a qualified agent, it may also include fiduciaries, corporations, partnerships, associations, and other entities named on a security, where such registration is authorized.

(c) "Paying agent(s)" or "agent(s)" refers to an eligible financial institution qualified under the provisions of this Circular to specially endorse securities and qualified under the provisions of Department of the Treasury Circular No. 750, current revision, to redeem eligible savings bonds and notes. The term includes branches of a qualified agent that redeem bonds and notes and account directly to a Federal Reserve Bank.

(d) "Redemption" and "payment" are used interchangeably for payment of a bond or note in accordance with the terms of its offering and the regulations governing it, and include "redemption-exchange".

(e) "Redemption-exchange" means any authorized redemption of eligible securities for the purpose of applying the proceeds in payment for other securities offered in exchange by the Treasury.

(f) "Savings bond(s)" or "bond(s)" means a United States Savings Bond of Series A, B, C, D, E, or EE.

(g) "Savings note(s)" or "note(s)" means a United States Savings Note (Freedom Share).



(h) "Security" or "securities" means a savings bond or note as defined in (f) and (g) of this section.

(i) "Special endorsement" means a procedure under which a security is redeemed by an agent, qualified under the provisions of this Circular, for cash or on redemption-exchange utilizing a special stamp placed on the security in lieu of a request for payment signed by the owner or coowner.

### § 330.2 Qualification for use of special endorsement.

(a) *Application for authority.* Any financial institution qualified as a paying agent of savings bonds and notes under the provisions of Department of the Treasury Circular No. 750, current revision, may establish its eligibility to employ the special endorsement procedure by executing and submitting the appropriate application-agreement form to the Federal Reserve Bank. In executing the form, the agent certifies that, by duly executed resolution of its governing board or committee, it has been authorized to apply for the privilege of paying and processing securities in accordance with the provisions and conditions of Circular No. 888, including all supplements, amendments, and revisions, and any related instructions. If the application is approved, the Federal Reserve Bank will issue a certificate of qualification.

(b) *Agents previously qualified.* Institutions qualified under previous revisions of this Circular are authorized to continue to act without requalification. By so acting, they shall be subject to the terms and conditions of the previously executed application and these regulations in the same manner and to the same extent as though they had requalified hereunder.

(c) *Termination of qualification.* The Secretary of the Treasury reserves the right to withdraw the special endorsement authority from any institution at any time. Such authority will also be terminated at any time at the request of the institution. In either event, formal notice of the termination shall be given to the agent in writing by the Federal Reserve Bank.

### § 330.3 Special endorsement of securities.

(a) *Form of endorsement.* Each security processed under the provisions of this circular shall bear the following endorsement:

Request by owner and validity of transaction guaranteed in accordance with T.D. Circular No. 888, as revised.

(Name, location, and paying agent code number assigned by Federal Reserve Bank)

This endorsement must be legibly impressed in black or other dark-colored ink on the back of the security in the space provided for the owner to request payment.

(b) *Endorsement stamps.* Endorsement stamps may be obtained from the Federal Reserve Bank or, with its approval, purchased by the agent. Requests for stamps to be furnished or approved by the Bank must be made in writing by an officer of the institution. Stamps procured by an agent may not exceed a space bounded by 1 3/4 inches vertically and 3 inches horizontally. They must follow exactly the wording prescribed. They may also include space for the transaction date and the initials or signature of the officer or employee authorized to approve the transaction.

(c) *Coownership securities.* In the case of securities registered in coownership form, the agent shall indicate which coowner requested payment or exchange by encircling in black or other dark-colored ink the name of the coowner (or both coowners, if the request is joint) in the inscription on the face of the security.

(d) *Restrictions.* Under no circumstances shall the special endorsement procedure be used to give effect to a transfer, hypothecation or pledge of a security, or to permit payment to any person other than the owner or coowner. Violation of these provisions will be cause for withdrawal of an agent's authority to process securities under the special endorsement procedure, and may involve additional penalties if the circumstances warrant such action.

### § 330.4 Guaranty given to the United States.

By the act of paying or presenting to a Federal Reserve Bank for payment or exchange a security on which it has affixed the special endorsement, a paying agent shall be deemed to have (a) unconditionally guaranteed to the United States the

validity of the transaction, including the identification of the owner and the disposition of the proceeds or the new bonds, as the case may be, in accordance with the presenter's instructions; (b) assumed complete and unconditional liability to the United States for any loss which may be incurred by the United States as a result of the transaction; and (c) unconditionally agreed to make prompt reimbursement for the amount of any loss, upon request of the Department of the Treasury.

**§ 330.5 Evidence of owner's authorization to affix special endorsement.**

(a) *Form of authorization.* The Treasury does not prescribe the form or type of instructions an agent must obtain from each owner in order to use the special endorsement procedure. In the case of a redemption-exchange, the owner or coowner authorized to request the exchange (as specified in Circular No. 750, Section 321.8(b)), must sign the exchange subscription even though the securities are specially endorsed.

(b) *Securities in coownership or beneficiary form.* Securities registered in coownership or beneficiary form should be accepted for special endorsement only for immediate payment or exchange. Acceptance of bonds and notes for processing at some future date should be avoided as authority to utilize endorsement generally expires upon the death of the owner or coowner on whose behalf securities were to be paid.

(c) *Record of authorization.* Agents should maintain such records as may be necessary to establish the receipt of, and compliance with, instructions supporting the special endorsement. If the agent elects to make notations on the back of the securities to serve as a record, the Bureau of the Public Debt will undertake to produce, on request, a photocopy of such security at any time up to 10 years after the redemption date. However, the Bureau does not assume responsibility for the adequacy of such notations, for the legibility of any photocopy, or for failure to produce a photocopy from its records.

**§ 330.6 Securities eligible for special endorsement.**

(a) *General authority.* A qualified agent is authorized to affix the special endorsement to: (1) savings bonds of Series A, B, C, D, E, and EE and savings notes to be redeemed for cash, and (2) eligible savings bonds of Series E and EE and savings notes to be redeemed in exchange for Series HH bonds under the provisions of Circular No. 2-80.

(b) *Securities which may not be specially endorsed.* The special endorsement procedure may not be used in any case in which payment or exchange (1) is requested by a parent on behalf of a minor child named on the security, or by a surviving beneficiary; or (2) requires documentary evidence, under regulations contained in Circulars Nos. 530 and 3-80.

(c) *Securities owned by nonresident aliens.* As securities owned by a nonresident alien individual, or a nonresident foreign corporation, partnership, or association may be subject to the nonresident alien withholding tax, bonds and notes held or received by an agent for the account of such owners must be forwarded to the Federal Reserve Bank for redemption, even though the agent may specially endorse the securities.

**§ 330.7 Payment or redemption-exchange by agent.**

Specially endorsed securities may be paid in cash or redeemed in exchange for Series HH bonds pursuant to the authority and subject, in all other respects, to the provisions of Circular No. 750, current revision, its Appendix, and any other instructions issued under its authority. Each specially endorsed bond or note paid by an agent must have the agent's payment stamp imprinted on its face and show the date and amount paid. Securities so paid should be combined with other securities paid under that Circular and forwarded to the Federal Reserve Bank for settlement. Securities redeemed on exchange must be accompanied by an exchange subscription and a remittance covering the issue price of the Series HH bonds.

**§ 330.8 Payment or redemption-exchange by Federal Reserve Bank.**

Specially endorsed securities which an agent is not authorized to redeem for cash or on exchange should be forwarded to the Federal Reserve Bank. The transmittals must be accompanied by appropriate instructions governing the transaction and the

disposition of the redemption checks or new bonds, as the case may be. The securities must be kept separate from others the agent has paid and must be submitted in accordance with instructions issued by the Bank.

### § 330.9 Fiscal agents.

The Federal Reserve Banks, as fiscal agents of the United States, are authorized to perform such services as may be requested by the Secretary of the Treasury or by his delegate, the Commissioner of the Public Debt, in connection with this Circular.

### § 330.10 Modifications of other Circulars.

The provisions of this Circular shall be considered as amending and supplementing: Department of the Treasury Circulars Nos. 530, 653, and 750, and Department of the Treasury Circulars, Public Debt Series Nos. 1-80, 2-80, 3-80, and 3-67, and any revisions thereof, and those Circulars are hereby modified to the extent necessary to accord with the provisions of this Circular.

### § 330.11 Supplements, amendments, or revisions.

The Secretary of the Treasury may, at any time, or from time to time, revise, supplement, amend or withdraw, in whole or in part, the provisions of this Circular.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

## Exhibit 15.—Department Circular No. 1-63, regulations governing U. S. retirement plan bonds, Fifth Amendment

DEPARTMENT OF THE TREASURY,  
*Washington, July 8, 1980.*

**SUMMARY:** The purpose of this fifth amendment to the Regulations Governing United States Retirement Plan Bonds is to provide for an interest rate of 6.5 percent per annum, compounded semiannually, on bonds issued on or after August 1, 1979.

**EFFECTIVE DATE:** August 1, 1979.

**SUPPLEMENTARY INFORMATION:** United States Retirement Plan Bonds have been issued since 1963 as an investment option for self-employed individuals eligible to contribute to a "Keogh" (H.R. 10) retirement plan. This amendment to the offering of these bonds implements an earlier announcement made by the Secretary of the Treasury that bonds issued on or after August 1, 1979, will accrue interest at the rate of 6.5 percent per annum, compounded semiannually. Section 341.1 of the offering is being amended accordingly, and a new table of redemption values, based on the 6.5 percent rate, is being added to the Appendix.

Since this amendment involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary. Accordingly, under authority of Sections 1 and 20 of the Second Liberty Bond Act, as amended (40 Stat. 288, 48 Stat 343, both as amended; 31 U.S.C. 752, 754b), and 5 U.S.C. 301, Department of the Treasury Circular, Public Debt Series No. 1-63, as amended, is hereby further amended as follows, effective August 1, 1979.

1. In § 341.1(a), paragraph (4) is revised and paragraph (5) is added, to read as follows:

### § 341.1 (Amended)

\* \* \* \* \*

(a) \* \* \*

(4) Bonds with the issue dates of February 1, 1974, through July 1, 1979—6 percent per annum compounded semiannually. (See Table C, appended to the third amendment of this Circular).



(5) Bonds with the issue date of August 1, 1979, or thereafter—6.5 percent per annum, compounded semiannually. (See Table D, appended to this amendment).

\* \* \* \* \*

2. In the Appendix, Table D is added as follows:

**Table D.—Table of Redemption Values Providing an Investment Yield of 6.50 Percent Per Annum for Bonds Bearing Issue Dates Beginning Aug. 1, 1979**

Table shows the increase in redemption value for each successive half-year term of holding following the date of issue on Retirement Plan Bonds bearing issue dates beginning August 1, 1979. The redemption values have been determined to provide an investment yield of approximately 6.50 percent<sup>1</sup> per annum, compounded semi-annually, on the purchase price from issue date to the beginning of each half-year period. The period to maturity is indeterminate in accordance with the provisions of Sec. 341.1(b) of this circular.<sup>2</sup>

Issue price.....	\$50	\$100	\$500	\$1,000
Period after issue date	Redemption values during each half-year period (values increase on first day of period shown)			
First ½ year.....	\$50.00	\$100.00	\$500.00	\$1,000.00
½ to 1 year.....	51.62	103.24	516.20	1,032.40
1 to 1 ½ years.....	53.30	106.60	533.00	1,066.00
1 ½ to 2 years.....	55.04	110.08	550.40	1,100.80
2 to 2 ½ years.....	56.82	113.64	568.20	1,136.40
2 ½ to 3 years.....	58.68	117.36	586.80	1,173.60
3 to 3 ½ years.....	60.58	121.16	605.80	1,211.60
3 ½ to 4 years.....	62.54	125.08	625.40	1,250.80
4 to 4 ½ years.....	64.58	129.16	645.80	1,291.60
4 ½ to 5 years.....	66.68	133.36	666.80	1,333.60
5 to 5 ½ years.....	68.84	137.68	688.40	1,376.80
5 ½ to 6 years.....	71.08	142.16	710.80	1,421.60
6 to 6 ½ years.....	73.40	146.80	734.00	1,468.00
6 ½ to 7 years.....	75.78	151.56	757.80	1,515.60
7 to 7 ½ years.....	78.24	156.48	782.40	1,564.80
7 ½ to 8 years.....	80.78	161.56	807.80	1,615.60
8 to 8 ½ years.....	83.40	166.80	834.00	1,668.00
8 ½ to 9 years.....	86.12	172.24	861.20	1,722.40
9 to 9 ½ years.....	88.92	177.84	889.20	1,778.40
9 ½ to 10 years.....	91.80	183.60	918.00	1,836.00
10 to 10 ½ years.....	94.80	189.60	948.00	1,896.00
10 ½ to 11 years.....	97.88	195.76	978.80	1,957.60
11 to 11 ½ years.....	101.06	202.12	1,010.60	2,021.20
11 ½ to 12 years.....	104.34	208.68	1,043.40	2,086.80
12 to 12 ½ years.....	107.72	215.44	1,077.20	2,154.40
12 ½ to 13 years.....	111.22	222.44	1,112.20	2,224.40
13 to 13 ½ years.....	114.84	229.68	1,148.40	2,296.80
13 ½ to 14 years.....	118.58	237.16	1,185.80	2,371.60
14 to 14 ½ years.....	122.44	244.88	1,224.40	2,448.80
14 ½ to 15 years.....	126.42	252.84	1,264.20	2,528.40
15 to 15 ½ years.....	130.52	261.04	1,305.20	2,610.40
15 ½ to 16 years.....	134.76	269.52	1,347.60	2,695.20
16 to 16 ½ years.....	139.14	278.28	1,391.40	2,782.80
16 ½ to 17 years.....	143.66	287.32	1,436.60	2,873.20
17 to 17 ½ years.....	148.34	296.68	1,483.40	2,966.80
17 ½ to 18 years.....	153.16	306.32	1,531.60	3,063.20
18 to 18 ½ years.....	158.12	316.24	1,581.20	3,162.40
18 ½ to 19 years.....	163.26	326.52	1,632.60	3,265.20
19 to 19 ½ years.....	168.58	337.16	1,685.80	3,371.60
19 ½ to 20 years.....	174.06	348.12	1,740.60	3,481.20
20 to 20 ½ years.....	179.72	359.44	1,797.20	3,594.40

<sup>1</sup> Based on redemption values of \$1,000 bond.

<sup>2</sup> At a future date prior to Aug. 1, 1999 (20 years after issue date of the first bonds) this table will be extended to show redemption values for periods of holding of 20 ½ years and beyond.

PAUL H. TAYLOR,  
Fiscal Assistant Secretary.

**Exhibit 16.—Department Circular No. 1-75, regulations governing U. S. individual retirement bonds, Second amendment**

DEPARTMENT OF THE TREASURY,  
Washington, July 8, 1980.

**SUMMARY:** The purpose of this second amendment to the Regulations Governing United States Individual Retirement Bonds is to provide for an interest rate of 6.5 percent per annum, compounded semiannually, to be paid on bonds issued on or after August 1, 1979.

**EFFECTIVE DATE:** August 1, 1979.

**SUPPLEMENTARY INFORMATION:** United States Individual Retirement Bonds have been issued since 1975 as an investment option for individuals eligible to contribute to an Individual Retirement Account (IRA). This amendment to the offering of these bonds implements an earlier announcement made by the Secretary of the Treasury that bonds issued on or after August 1, 1979, will accrue interest at the rate of 6.5 percent per annum, compounded semiannually. Section 346.1 of the offering is being amended accordingly, and a new table of redemption values, based on the 6.5 percent rate, is being added to the Appendix.

Since this amendment involves the fiscal policy of the United States and does not meet the Department's criteria for significant regulations, it has been determined that notice and public procedures are unnecessary. Accordingly, under authority of Sections 1 and 20 of the Second Liberty Bond Act, as amended (40 Stat. 288, 48 Stat 343, both as amended; 31 U.S.C. 752, 754b), and 5 U.S.C. 301, Department of the Treasury Circular, Public Debt Series No. 1-75, as amended, is hereby further amended as follows, effective August 1, 1979.

1. In § 346.1, paragraph (a) is revised to read as follows:

**§ 346.1 [Amended]**

\* \* \* \* \*

(a) *Investment yield (interest).* United States Individual Retirement Bonds, hereinafter sometimes referred to as Individual Retirement Bonds, will be issued at par. The investment yields (interest) are as follows:

(1) Bonds with the issue dates of January 1, 1975, through July 1, 1979—6 percent per annum compounded semiannually. (See Table of Redemption Values appended to the Circular.)

(2) Bonds with the issue date of August 1, 1979, or thereafter—6.5 percent per annum, compounded semiannually. (See Table A appended to this amendment.) Interest will be paid only upon redemption of the bonds. The accrual of interest will continue until the bonds have been redeemed or have reached maturity, whichever is earlier, in accordance with these regulations.

\* \* \* \* \*

2. In the Appendix, Table A is added as follows:

**Table A.—Table of Redemption Values Providing an Investment Yield of 6.50 Percent Per Annum for Bonds Bearing Issue Dates Beginning Aug. 1, 1979.**

**Note.**—This table shows how Individual Retirement Bonds bearing issue dates on or after August 1, 1979, by denomination, increase in redemption value during the successive half-year periods following issue. The redemption values provide an investment yield of approximately 6.50 percent per annum, compounded semiannually, on the purchase price from issue date to the

beginning of each half-year period. No increase in redemption value is shown, however, until 1 year after issue date since no interest may be paid on bonds redeemed before that time. The period to maturity is fixed in accordance with the provisions of Sec. 346.1(b) of this circular.

Issue price .....	\$50	\$75	\$100	\$500
Period after issue date .....	Redemption values during each half-year period (values increase on first day of period shown)			
1st year .....	\$50.00	\$75.00	\$100.00	\$500.00
1 to 1 ½ years .....	53.30	79.95	106.60	533.00
1 ½ to 2 years .....	55.04	82.56	110.08	550.40
2 to 2 ½ years .....	56.82	85.23	113.64	568.20
2 ½ to 3 years .....	58.68	88.02	117.36	586.80
3 to 3 ½ years .....	60.58	90.87	121.16	605.80
3 ½ to 4 years .....	62.54	93.81	125.08	625.40
4 to 4 ½ years .....	64.58	96.87	129.16	645.80
4 ½ to 5 years .....	66.68	100.02	133.36	666.80
5 to 5 ½ years .....	68.84	103.26	137.68	688.40
5 ½ to 6 years .....	71.08	106.62	142.16	710.80
6 to 6 ½ years .....	73.40	110.10	146.80	734.00
6 ½ to 7 years .....	75.78	113.67	151.56	757.80
7 to 7 ½ years .....	78.24	117.36	156.48	782.40
7 ½ to 8 years .....	80.78	121.17	161.56	807.80
8 to 8 ½ years .....	83.40	125.10	166.80	834.00
8 ½ to 9 years .....	86.12	129.18	172.24	861.20
9 to 9 ½ years .....	88.92	133.38	177.84	889.20
9 ½ to 10 years .....	91.80	137.70	183.60	918.00
10 to 10 ½ years .....	94.80	142.20	189.60	948.00
10 ½ to 11 years .....	97.88	146.82	195.76	978.80
11 to 11 ½ years .....	101.06	151.59	202.12	1,010.60
11 ½ to 12 years .....	104.34	156.51	208.68	1,043.40
12 to 12 ½ years .....	107.72	161.58	215.44	1,077.20
12 ½ to 13 years .....	111.22	166.83	222.44	1,112.20
13 to 13 ½ years .....	114.84	172.26	229.68	1,148.40
13 ½ to 14 years .....	118.58	177.87	237.16	1,185.80
14 to 14 ½ years .....	122.44	183.66	244.88	1,224.40
14 ½ to 15 years .....	126.42	189.63	252.84	1,264.20
15 to 15 ½ years .....	130.52	195.78	261.04	1,305.20
15 ½ to 16 years .....	134.76	202.14	269.52	1,347.60
16 to 16 ½ years .....	139.14	208.71	278.28	1,391.40
16 ½ to 17 years .....	143.66	215.49	287.32	1,436.60
17 to 17 ½ years .....	148.34	222.51	296.68	1,483.40
17 ½ to 18 years .....	153.16	229.74	306.32	1,531.60
18 to 18 ½ years .....	158.12	237.18	316.24	1,581.20
18 ½ to 19 years .....	163.26	244.89	326.52	1,632.60
19 to 19 ½ years .....	168.58	252.87	337.16	1,685.80
19 ½ to 20 years .....	174.06	261.09	348.12	1,740.60
20 to 20 ½ years .....	179.72	269.58	359.44	1,797.20

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

**Exhibit 17.—Department Circular No. 530, regulations governing U. S. savings bonds, Series A, B, C, D, E, F, G, H, J, and K, and U. S. savings notes, 11th Revision**

DEPARTMENT OF THE TREASURY,  
*Washington, September 11, 1980.*

**SUMMARY:** The Department of the Treasury hereby issues final regulations governing United States Savings Bonds of Series A, B, C, D, E, F, G, J, and K, and United States Savings Notes. The regulations revise those found in Department of the Treasury Circular No. 530, Tenth Revision (31 CFR, Part 315).

The changes made reflect the withdrawal from sale of Series E and H savings bonds, and parallel, to the extent legally feasible, the format and content of the regulations governing Series EE and HH savings bonds.

**EFFECTIVE DATE:** October 1, 1980.



**SUPPLEMENTARY INFORMATION:** All series of the United States Savings Bonds, except Series EE and HH, and all United States Savings Notes have been governed by regulations published in Department of the Treasury Circular No. 530 (31 CFR, Part 315), hereafter referred to as Circular No. 530.

The individual series of bonds and notes subject to that Circular were issued pursuant to the terms and conditions of the following offering circulars, including any revisions and amendments:

Series	Department of the Treasury Circular No.
A.....	529.
B.....	554.
C.....	571.
D.....	596.
E.....	653.
F.....	654.
G.....	654.
H.....	905 and 1036.
J.....	906.
K.....	906.
Savings Notes .....	Public Debt Series No. 3-67.

All of these securities have now been withdrawn from sale. The offering circulars covering Series E and H bonds and savings notes provide that these securities may be held for optional extension periods beyond their original maturities during which they will continue to earn interest.

On June 27, 1980, the Department of the Treasury published in proposed form an Eleventh Revision of Circular No. 530. The public was invited to submit written comments on the proposed regulations on or before August 1, 1980. No comments were received.

The Eleventh Revision of Circular No. 530 was drafted to conform as closely as possible to the regulations governing Series EE and HH savings bonds, which were offered for sale as of January 1, 1980. Those regulations are contained in Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR, Part 353), published in the Federal Register on December 26, 1979, pages 76440 through 76455.

The ways in which the Eleventh Revision of Circular No. 530 differ from the Tenth Revision are discussed in the following paragraphs:

### General

The regulations in Circular No. 530 are divided into subparts and sections numbered by reference to Part 315 under which the Circular appears in Title 31 of the Code of Federal Regulations. To avoid repetitious citations in the explanations that follow, reference will be made only to subparts or section numbers of Circular No. 530, without parenthetical CFR references.

### Application of Regulations

Section 315.0. This section explains that the rules in the Eleventh Revision of Circular No. 530 apply to all series of United States Savings Bonds, except Series EE and HH, and to all United States Savings Notes.

### Definitions

Section 315.2. The definitions in the Tenth Revision of Circular No. 530 have been conformed to those appearing in Circular No. 3-80.

### Registration

Subpart B. Although the sale of all bonds and notes governed by Circular No. 530 has been discontinued, the provisions relating to registration on original issue have been retained for reference purposes. For the sake of clarity, the Subpart has been rearranged under new headings, but the contents remain relatively unchanged.

Section 315.5 no longer contains the general prohibition against the designation of attorneys-in-fact for the purpose of requesting payment. Limited acceptance of powers of attorney is now authorized under conditions specified in § § 315.40(d) and 315.65.

### Adjudication of Claims

Subpart F. The only substantive change in this Subpart is the addition of a new § 315.29 relating to the adjudication of claims for lost, stolen or destroyed savings bonds and notes.

In the ordinary course of business, the Bureau of the Public Debt creates records that reflect the status of each savings bond and note manufactured and delivered to the Bureau. Supplementing these are records, principally on microfilm, that show the registration and other essential data for each security issued and retired, including the signature to the request for payment on each redeemed security.

The proliferation of detailed records encompassing some 5 billion individual securities issued over a period of 45 years has created storage and other administrative problems, and has resulted in steadily rising costs. Changes in the adjudication process that are outlined below will permit the Bureau to eliminate a number of these detailed records without affecting its ultimate ability to adjudicate claims for relief or unduly impairing the rights of individual security owners. The changes described below are effective as of December 1, 1980.

First, photocopies of bonds and notes showing the signature to the request for payment will not be supplied to any person who files a claim on account of a security more than 10 years after the date of its redemption, based on the records of the Bureau of the Public Debt. This will not bar the acceptance and adjudication of any claim on the basis of the facts presented and other Bureau records.

Second, no claim for any savings bond or note that is filed six or more years after the final maturity of the security will be accepted and adjudicated unless the claimant can furnish the serial number of the security. Records retained beyond six years from a security's final maturity can be accessed only by serial number.

Holders of savings bonds and notes have always been encouraged to keep lists of their securities by serial numbers in a place apart from the securities. The information facilitates the adjudication of claims in all cases. This practice becomes increasingly important as Bureau records are disposed of in compliance with Federal records retention standards.

### Interest

Subpart G. The rules covering payment of interest on Series E bonds in § 315.30 have been rewritten for purposes of clarification. Section 315.31, covering Series H interest, has been subdivided and subheads have been added.

### Payment

Subpart H. This Subpart brings together all general provisions relating to the payment of bonds and notes which were found in Subparts L, M, and N in previous revisions of the Circular.

The following changes in organization have been made to group the rules in a clearer, more logical order:

Eleventh revision	Appeared in tenth revision
Section 315.39(a).....	Section 315.38(b).
Section 315.39(b).....	Section 315.38(a).
Section 315.39(c).....	Section 315.37(b).
Section 315.40(a), (b), (c) .....	Section 315.37(a), (c).

Section 315.40(d) is new and provides that attorneys-in-fact may request payment of bonds belonging to the grantor of a power of attorney if the power was executed before an authorized certifying officer and specifically covers the sale of Treasury securities.

The rules on the use of a power of attorney in the case of a grantor who has become incompetent or physically disabled appear in § 315.65. These rules require that the power specifically provide that the authority granted will not be affected by the subsequent incapacity of the grantor.

### Reissue

Subpart I. As in Subpart H, the principal changes in this Subpart result from the reorganization of the material relating to reissue previously found in Subparts L, M, and N.

For certain types of reissue, the parties involved must be related. The degree of that relationship is no longer specified in the Eleventh Revision; rather, the rules apply to any relationship by blood, adoption, or marriage.

Section 315.47(b). This paragraph introduces two slight modifications of previous rules for the reissue of savings bonds and notes registered in coownership form. The changes deal with cases involving the removal of the name(s) of either or both coowners and the designation of a third individual as owner, coowner, or beneficiary. This minor revision brings the rules for Series E and H bonds and savings notes into conformity with the rule for Series EE and HH bonds.

Section 315.47(c). This section is substantially the same as § 315.66 in the Tenth Revision. It should be noted that there is no change in the requirement that a beneficiary's name may not be removed from a bond or note while the beneficiary is living, without the beneficiary's consent. This rule has been in effect since savings bonds were first issued and continues to apply to all series of bonds and notes governed by Circular No. 530. Courts have held that under the provisions of the regulations, by virtue of the registration of a security in beneficiary form, the beneficiary acquires vested rights in the security. These rights are spelled out in the regulations. The provision requiring the beneficiary's written consent to the removal of his or her name from a security has not been carried over into the regulations governing Series EE and HH bonds. However, it is continued for all outstanding Series E and H bonds and savings notes because it is a part of the contract under which they were issued and applies uniformly to all such securities.

### Certifying Officers

Subpart J. The list of officers authorized to certify requests for payment, reissue, and other transactions has been revised to delete the names of certain designees who seldom, if ever, provide the service. One change involves the termination of the certification services of post offices, since they no longer issue savings bonds.

### Small Estates

Subpart L. Section 315.73(b) of the Tenth Revision provides that persons entitled to share in the estate of a deceased sole owner of savings bonds or notes whose estate is not being administered may, by joint agreement, request disposition of the bonds or notes.

To simplify the disposition of bonds and notes in amounts not exceeding \$1,000 (face amount), § 315.72(d) of the Eleventh Revision establishes a new procedure under which payment of bonds may be made to certain classes of survivors, without the necessity of the agreement of all other persons who might have an interest in the decedent's estate under State law.

The Fiscal Service issues the following regulations to govern all series of United States Savings Bonds of Series A, B, C, D, E, F, G, H, J, and K, and all United States Savings Notes.

Part 315 of Title 31 CFR is revised as follows:

#### SUBPART A—GENERAL INFORMATION

#### § 315.0 Applicability.

The regulations in this circular, Department of the Treasury Circular No. 530, and the provisions of the respective offering circulars, govern—



(a) United States Savings Bonds of Series E and Series H and United States Savings Notes, and

(b) United States Savings Bonds of Series A, B, C, D, F, G, J, and K, all of which have been matured and are no longer earning interest.

The regulations in Department of the Treasury Circular, Public Debt Series No. 3-80 (31 CFR, Part 353), govern United States Savings Bonds of Series EE and Series HH.

### § 315.1 Official agencies.

(a) The Bureau of the Public Debt of the Department of the Treasury is responsible for administering the Savings Bonds Program. Authority to process most transactions has been delegated to Federal Reserve Banks and Branches, as fiscal agents of the United States.

(b) Communications concerning transactions and requests for forms should be addressed to (1) a Federal Reserve Bank or Branch; (2) the Bureau of the Public Debt, 200 Third Street, Parkersburg, West Virginia 26101; or (3) the Bureau of the Public Debt, Washington, D.C. 20226. Notices and documents must be filed with these agencies, as provided in these regulations. The names and addresses of the Federal Reserve Banks and Branches are:

Federal Reserve Bank of Boston, Boston, Massachusetts 02106.

Federal Reserve Bank of New York, Federal Reserve Post Office Station, New York, New York 10045. Buffalo Branch, Federal Reserve Bank, Box 961, Buffalo, New York 14240.

Federal Reserve Bank of Philadelphia, Box 77, Philadelphia, Pennsylvania 19105.

Federal Reserve Bank of Cleveland, Box 6387, Cleveland, Ohio 44101. Cincinnati Branch, Federal Reserve Bank, Box 999, Cincinnati, Ohio 45201. Pittsburgh Branch, Federal Reserve Bank, Box 867, Pittsburgh, Pennsylvania 15230.

Federal Reserve Bank of Richmond, Box 27622, Richmond, Virginia 23261. Baltimore Branch, Federal Reserve Bank, Box 1378, Baltimore, Maryland 21203. Charlotte Branch, Federal Reserve Bank, Box 300, Charlotte, North Carolina 28230.

Federal Reserve Bank of Atlanta, Atlanta, Georgia 30303. Birmingham Branch, Federal Reserve Bank, Box 10447, Birmingham, Alabama 35202. Jacksonville Branch, Federal Reserve Bank, Jacksonville, Florida 32203. Miami Branch, Federal Reserve Bank, Box 520847, Miami, Florida 33152. Nashville Branch, Federal Reserve Bank, Nashville, Tennessee 37203. New Orleans Branch, Federal Reserve Bank, Box 61630, New Orleans, Louisiana 70161.

Federal Reserve Bank of Chicago, Box 834, Chicago, Illinois 60690. Detroit Branch, Federal Reserve Bank, Box 1059, Detroit, Michigan 48231.

Federal Reserve Bank of St. Louis, Box 442, St. Louis, Missouri 63166. Little Rock Branch, Federal Reserve Bank, Box 1261, Little Rock, Arkansas 72203. Louisville Branch, Federal Reserve Bank, Box 32710, Louisville, Kentucky 40232. Memphis Branch, Federal Reserve Bank, Box 407, Memphis, Tennessee 38101.

Federal Reserve Bank of Minneapolis, Minneapolis, Minnesota 55480. Helena Branch, Federal Reserve Bank, Helena, Montana 59601.

Federal Reserve Bank of Kansas City, Federal Reserve Station, Kansas City, Missouri 64198. Denver Branch, Federal Reserve Bank, Box 5228, Terminal Annex, Denver, Colorado 80217. Oklahoma City Branch, Federal Reserve Bank, Box 25129, Oklahoma City, Oklahoma 73125. Omaha Branch, Federal Reserve Bank, Omaha, Nebraska 68102.

Federal Reserve Bank of Dallas, Station K, Dallas, Texas 75222. El Paso Branch, Federal Reserve Bank, Box 100, El Paso, Texas 79999. Houston Branch, Federal Reserve Bank, Box 2578, Houston, Texas 77001. San Antonio Branch, Federal Reserve Bank, Box 1471, San Antonio, Texas 78295.

Federal Reserve Bank of San Francisco, Box 7702, San Francisco, California 94120. Los Angeles Branch, Federal Reserve Bank, Box 2077, Terminal Annex, Los Angeles, California 90051. Portland Branch, Federal Reserve Bank, Box 3436, Portland, Oregon 97208. Salt Lake City Branch, Federal Reserve Bank, Box 30780, Salt Lake City, Utah 84125. Seattle Branch, Federal Reserve Bank, Box 3567, Seattle, Washington 98124.

### § 315.2 Definitions.

As used in these regulations—

(a) “Bond” means a United States Savings Bond of any series except EE and HH, unless the context indicates otherwise. General references to bonds and direct references to Series E bonds also include United States Savings Notes, unless specifically excluded.

(b) “Extended maturity period” means any period after the original maturity date during which the owner may retain a bond and continue to earn interest on the maturity value or extended maturity value under applicable provisions of the circular offering the bond for sale.

(c) “Extended maturity value” is the value of a bond at the end of the applicable extended maturity period.

(d) “Final extended maturity date” is the date on which a bond will mature and cease to bear interest at the end of the final extended maturity period.

(e) “Incompetent” means an individual who is incapable of handling his or her business affairs because of a legal, mental or medically-established physical disability, except that a minor is not an incompetent solely because of age.

(f) “Issuing agent” means an organization that has been qualified under the provisions of Department of the Treasury Circular, Public Debt Series No. 4-67, current revision (31 CFR, Part 317), to issue savings bonds.

(g) “Original maturity date” means the date on which the bond reaches the end of the term for which it was initially offered and, unless further extended, ceases to earn interest.

(h) “Paying agent” means a financial institution that has been qualified under the provisions of Department of the Treasury Circular No. 750, current revision (31 CFR, Part 321), to make payment of savings bonds.

(i) “Payment” means redemption, unless otherwise indicated by context.

(j) “Person” means any legal entity including, but without limitation, an individual, corporation (public or private), partnership, unincorporated association, or fiduciary estate.

(k) “Personal trust estates” means trust estates established by natural persons in their own right for the benefit of themselves or other natural persons in whole or in part, and common trust funds comprised in whole or in part of such trust estates.

(l) “Reissue” means the cancellation and retirement of a bond and the issuance of a new bond or bonds of the same series, same issue date, and same total face amount.

(m) “Representative of the estate of a minor, incompetent, aged person, absentee, et al.” means the court-appointed or otherwise qualified person, regardless of title, who is legally authorized to act for the individual. The term does not include parents in their own right, voluntary or natural guardians, or the executors or administrators of decedents’ estates.

(n) “Surrender” means the actual receipt of a bond with an appropriate request for payment or reissue by either a Federal Reserve Bank or Branch, the Bureau of the Public Debt, or, if a paying agent is authorized to handle the transaction, the actual receipt of the bond and the request for payment by the paying agent.

(o) “Taxpayer identifying number” means a social security account number or an employer identification number.

(p) “Voluntary guardian” means an individual who is recognized as authorized to act for an incompetent, as provided by § 315.64.

## SUBPART B—REGISTRATION

## § 315.5 General rules.

(a) *Registration is conclusive of ownership.* Savings bonds are issued only in registered form. The registration must express the actual ownership of, and interest in, the bond. The registration is conclusive of ownership, except as provided in § 315.49.

(b) *Requests for registration.* Registrations requested must be clear, accurate and complete, conform substantially with one of the forms set forth in this Subpart, and include the taxpayer identifying number of the owner or first-named coowner. The taxpayer identifying number of the second-named coowner or beneficiary is not required but its inclusion is desirable. The registration of all bonds owned by the same person, organization, or fiduciary should be uniform with respect to the name of the owner and any description of the fiduciary capacity. An individual should be designated by the name he or she is ordinarily known by or uses in business, including at least one full given name. The name may be preceded or followed by any applicable title, such as 'Miss', 'Mr.', 'Mrs.', 'Ms.', 'Dr.', 'Rev.', 'M.D.', or 'D.D.'. A suffix, such as 'Sr.' or 'Jr.', must be included when ordinarily used or when necessary to distinguish the owner from another member of his family. A married woman's own given name, not that of her husband, must be used; for example, 'Mary A. Jones' or 'Mrs. Mary A. Jones,' NOT 'Mrs. Frank B. Jones.' The address must include, where appropriate, the number and street, route, or any other local feature, city, State, and ZIP Code.

## § 315.6 Restrictions on registration.

(a) *Natural persons.* Only an individual in his or her own right may be designated as coowner or beneficiary along with any other individual, whether on original issue or reissue, except as provided in § 315.7(g).

(b) *Residence.* The designation of an owner or first-named coowner is restricted, on original issue only, to persons (whether individuals or others) who are—

(1) Residents of the United States, its territories and possessions, the Commonwealth of Puerto Rico, and the former Canal Zone;

(2) Citizens of the United States residing abroad;

(3) Civilian employees of the United States or members of its armed forces, regardless of their residence or citizenship; and

(4) Residents of Canada or Mexico who work in the United States but only if the bonds are purchased on a payroll deduction plan and the owner provides a taxpayer identifying number. A nonresident alien may be designated coowner or beneficiary or, on authorized reissue, owner, unless the nonresident alien is a resident of an area with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States or its agencies or instrumentalities. See Department of the Treasury Circular No. 655, current revision (31 CFR, Part 211). Registration is not permitted in any form which includes the name of any alien who is a resident of any restricted area.

(c) *Minors.*

(1) Minors may purchase with their wages, earnings, or other funds belonging to them and under their control bonds registered in their names alone or with a coowner or beneficiary.

(2) Bonds purchased by another person with funds belonging to a minor not under legal guardianship or similar fiduciary estate must be registered, without a coowner or beneficiary, in the name of the minor or a natural guardian on behalf of a minor.

(3) Bonds purchased with funds of another may be registered to name the minor as owner, coowner, or beneficiary. If the minor is under legal guardianship or similar fiduciary estate, the registration must include an appropriate reference to it.

(4) Bonds purchased as a gift to a minor under a gifts-to-minors statute must be registered as prescribed by the statute and no coowner or beneficiary may be named.

(5) Bonds purchased by a representative of a minor's estate must be registered in the name of the minor and must include in the registration an appropriate reference to the guardianship or similar fiduciary estate. Bonds purchased by a representative of the estates of two or more minors, even though appointed in a single proceeding, must be



registered in the name of each minor separately with appropriate reference to the guardianship or similar fiduciary estate.

(d) *Incompetents.* Bonds may be registered to name as owner, coowner, or beneficiary an incompetent for whose estate a guardian or similar representative has been appointed, except that a coowner or beneficiary may not be named on bonds purchased with funds belonging to the incompetent. The registration must include appropriate reference to the guardianship or similar fiduciary estate. Bonds should not be registered in the name of an incompetent unless there is a representative for his or her estate, except as provided in § 315.64.

### § 315.7 Authorized forms of registration.

(a) *General.* Subject to any limitations or restrictions contained in these regulations on the right of any person to be named as owner, coowner, or beneficiary, bonds should be registered as indicated below. A savings bond inscribed in a form not substantially in agreement with one of the forms authorized by this Subpart is not considered validly issued.

(b) *Natural persons.* A bond may be registered in the names of individuals in their own right, but only in one of the forms authorized by this paragraph.

(1) *Single ownership form.* A bond may be registered in the name of one individual. Example:

John A. Jones 123-45-6789.

(2) *Coownership form.* A bond may be registered in the names of two individuals in the alternative as coowners. The form of registration "A and B" is not authorized. Examples:

John A. Jones 123-45-6789 or Ella S. Jones 987-65-4321.

John A. Jones 123-45-6789 or (Miss, Ms. or Mrs.) Ella S. Jones.

Ella S. Jones 987-65-4321 or John A. Jones.

(3) *Beneficiary form.* A bond may be registered in the name of one individual payable on death to another. "Payable on death to" may be abbreviated to "P.O.D." Examples:

John A. Jones 123-45-6789 payable on death to Mrs. Ella S. Jones.

John A. Jones 123-45-6789 P.O.D. Ella S. Jones 987-65-4321.

(c) *Fiduciaries (including legal guardians and similar representatives, certain custodians, natural guardians, executors, administrators, and trustees).*

(1) *General.* A bond may be registered in the name of any person or persons or any organization acting as fiduciary of a single fiduciary estate, but not where the fiduciary will hold the bond merely or principally as security for the performance of a duty, obligation, or service. Registration should conform to a form authorized by this paragraph. A coowner or beneficiary may be named only in accordance with the applicable provisions of § 315.6(c) and (d). A common trust fund established and maintained by a financial institution authorized to act as a fiduciary will be considered a single fiduciary estate within the meaning of these regulations.

(2) *Legal guardians, conservators, similar representatives, certain custodians.* A bond may be registered in the name and title or capacity of the legally appointed or authorized representative of the estate of a minor, incompetent, aged or infirm person, absentee, et al., or in the name of that individual followed by an appropriate reference to the estate. Examples:

Tenth National Bank, guardian (or conservator, trustee, etc.) of the estate of George N. Brown 123-45-6789, a minor (or an incompetent, aged person, infirm person, or absentee).

Henry C. Smith, conservator of the estate of John R. White 123-45-6789, an adult, pursuant to Sec. 633.572 of the Iowa Code.

John F. Green 123-45-6789, a minor (or an incompetent) under custodianship by designation of the Veterans Administration.

Fra. k M. Redd 123-45-6789, an incompetent for whom Eric A. Redd has been designated trustee by the Department of the Army pursuant to 37 U.S.C. 602.

Arnold A. Ames, as custodian for Barry B. Bryan 123-45-6789, under the California Uniform Gifts to Minors Act.

Thomas C. Reed, as custodian for Lawrence W. Reed 123-45-6789, a minor, under the laws of Georgia.

Richard A. Rowe 123-45-6789, for whom Reba L. Rowe is representative payee for social security benefits (or black lung benefits, as the case may be). (If the beneficiary is a minor, the words "a minor" should appear immediately after the social security number.)

Henry L. Green 123-45-6789 or George M. Brown, a minor under legal guardianship of the Tenth National Bank.

Henry L. Green 123-45-6789 P.O.D. George M. Brown, a minor under legal guardianship of the Tenth National Bank.

Redd State Hospital and School, selected payee for John A. Jones 123-45-6789, a Civil Service annuitant, pursuant to 5 U.S.C. 8345(e).

(3) *Natural guardians.* A bond may be registered in the name of either parent of a minor, as natural guardian. The registration of a bond in this form is considered as establishing a fiduciary relationship. A coowner or beneficiary may be named but only if the funds used to purchase the bond do not belong to the minor. Examples:

John A. Jones, as natural guardian for Henry M. Jones 123-45-6789.

Melba Smith, as natural guardian for Thelma Smith 123-45-6789 P.O.D.  
Bartholomew Smith.

(4) *Executors and administrators.* A bond may be registered in the name of the representative appointed by a court to act for an estate of a decedent, or in the name of an executor authorized to administer a trust under the terms of a will although not named trustee. The name and capacity of all the representatives as shown in the letters of appointment must be included in the registration and be followed by an adequate identifying reference to the estate. Examples:

John H. Smith and Calvin N. Jones, executors of the will (or administrators of the estate) of Robert J. Smith, deceased 12-3456789.

John H. Smith, executor of the will of Robert J. Smith, deceased, in trust for Mrs. Jane L. Smith, with remainder over 12-3456789.

(5) *Trustee or life tenants under wills, deeds of trust, agreements, or similar instruments.* A bond may be registered in the name and title of the trustee of a trust estate, or in the name of a life tenant, followed by an adequate identifying reference to the authority governing the trust or life tenancy. Examples:

Thomas J. White and Tenth National Bank, trustees under the will of Robert J. Smith, deceased 12-3456789.

Jane N. Black 123-45-6789, life tenant under the will of Robert J. Black, deceased.

Tenth National Bank, trustee under agreement with Paul E. White, dated 2/1/76, 12-3456789.

Carl A. Black and Henry B. Green, trustees under agreement with Paul E. White, dated 2/1/76, 12-3456789.

Paul E. White, trustee under declaration of trust dated 2/1/76, 12-3456789.

(i) If the trust instrument designates by title only an officer of a board or an organization as trustee, only the title of the officer should be used. Example:

Chairman, Board of Trustees, First Church of Christ, Scientist, of Chicago, Illinois, in trust under the will of Robert J. Smith, deceased 12-3456789.

(ii) The names of all trustees, in the form used in the trust instrument, must be included in the registration, except as follows:

(A) If there are several trustees designated as a board or they are required to act as a unit, their names may be omitted and the words "Board of Trustees" substituted for the word "trustee". Example:

Board of Trustees of Immediate Relief Trust of Federal Aid Association, under trust indenture dated 2/1/76, 12-3456789.

(B) If the trustees do not constitute a board or are not required to act as a unit, and are too numerous to be designated in the registration by names and title, some or all the names may be omitted. Examples:

John A. Smith, Henry B. Jones, et al., trustees under the will of Edwin O. Mann, deceased 12-3456789.

Trustees under the will of Edwin O. Mann, deceased 12-3456789.

(6) *Employee thrift, savings, vacation and similar plans.* A bond may be registered in the name and title, or title alone, of the trustee of an eligible employee thrift, savings, vacation or similar plan, as defined in § 316.5, of Department of the Treasury Circular No. 653, current revision. If the instrument creating the trust provides that the trustees shall serve for a limited term, their names may be omitted. Examples:

Tenth National Bank, trustee of Pension Fund of Safety Manufacturing Company, U/A with the company, dated March 31, 1976, 12-3456789.

Trustees of Retirement Fund of Safety Manufacturing Company, under directors' resolution adopted March 31, 1976, 12-3456789.

County Trust Company, Trustee of the Employee Savings Plan of Jones Company, Inc., U/A dated January 17, 1976, 12-3456789.

Trustee of the Employee Savings Plan of Brown Brothers, Inc., U/A dated January 20, 1976, 12-3456789.

(7) *Funds of lodges, churches, societies, or similar organizations.* A bond may be registered in the title of the trustees, or a board of trustees, holding funds in trust for a lodge, church, or society, or similar organization, whether or not incorporated. Examples:

Trustees of the First Baptist Church, Akron, Ohio, acting as a Board under Section 15 of its bylaws 12-3456789.

Trustees of Jamestown Lodge No. 1000, Benevolent and Protective Order of Elks, under Section 10 of its bylaws 12-3456789.

Board of Trustees of Lotus Club, Washington, Indiana, under Article 10 of its constitution 12-3456789.

(8) *Investment agents for religious, educational, charitable and non-profit organizations.* A bond may be registered in the name of a bank, trust company, or other financial institution, or an individual, as agent under an agreement with a religious, educational, charitable or non-profit organization, whether or not incorporated, if the agent holds funds for the sole purpose of investing them and paying the income to the organization. The name and designation of the agent must be followed by an adequate reference to the agreement. Examples:

Tenth National Bank, fiscal agent U/A with the Evangelical Lutheran Church of the Holy Trinity, dated 12/28/76, 12-3456789.

Sixth Trust Company, Investment Agent U/A dated September 16, 1976, with Central City Post, Department of Illinois, American Legion, 12-3456789.

John Jones, Investment Agent U/A dated September 16, 1976, with Central City Post, Department of Illinois, American Legion, 12-3456789.

(9) *Funds of school groups or activities.* A bond may be registered in the title of the principal or other officer of a public, private, or parochial school holding funds in trust for a student body fund or for a class, group, or activity. If the amount purchased for any one fund does not exceed \$2,500 (face amount), no reference need be made to a trust instrument. Examples:

Principal, Western High School, in trust for the Class of 1976 Library Fund, 12-3456789.

Director of Athletics, Western High School, in trust for Student Activities Association, under resolution adopted 5/12/76, 12-3456789.

(10) *Public corporations, bodies, or officers as trustees.* A bond may be registered in the name of a public corporation or a public body, or in the title of a public officer, acting as trustee under express authority of law, followed by an appropriate reference to the statute creating the trust. Examples:

Rhode Island Investment Commission, trustee of the General Sinking Fund under Title 35, Ch. 8, Gen. Laws of Rhode Island.



Superintendent of the Austin State Hospital Annex, in trust for the Benefit Fund under Article 3183C, Vernon's Civ. Stat. of Texas Ann.

(d) *Private organizations (corporations, associations, partnerships).*

(1) *General.* A bond may be registered in the name of any private organization in its own right. The full legal name of the organization as set forth in its charter, articles of incorporation, constitution, partnership agreement, or other authority from which its powers are derived, must be included in the registration and may be followed by a parenthetical reference to a particular account other than a trust account.

(2) *Corporations.* A bond may be registered in the name of a business, fraternal, religious, non-profit, or other private corporation. The words "a corporation" must be included in the registration unless the fact of incorporation is shown in the name. Examples:

Smith Manufacturing Company, a corporation 12-3456789.

Green and Redd, Inc. 12-3456789 (Depreciation Acct.).

(3) *Unincorporated associations.* A bond may be registered in the name of a club, lodge, society, or a similar self-governing association which is unincorporated. The words "an unincorporated association" must be included in the registration. This form of registration must not be used for a trust fund, board of trustees, a partnership, or a sole proprietorship. If the association is chartered by or affiliated with a parent organization, the name or designation of the subordinate or local organization must be given first, followed by the name of the parent organization. The name of the parent organization may be placed in parentheses and, if well known, may be abbreviated. Examples:

The Lotus Club, an unincorporated association, 12-3456789.

Local 447, Brotherhood of Railroad Trainmen, an unincorporated association, 12-3456789.

Eureka Lodge 317 (A.F. and A.M.), an unincorporated association, 12-3456789.

(4) *Partnerships.* A bond may be registered in the name of a partnership. The words "a partnership" must be included in the registration. Examples:

Smith & Jones, a partnership, 12-3456789.

Acme Novelty Company, a partnership, 12-3456789.

(5) *Sole proprietorships.* A bond may be registered in the name of an individual who is doing business as a sole proprietor. A reference may be made to the trade name under which the business is conducted. Example:

John Jones d.b.a. Jones Roofing Company, 123-45-6789

(e) *Institutions (churches, hospitals, homes, schools, etc.).* A bond may be registered in the name of a church, hospital, home, school, or similar institution conducted by a private organization or by private trustees, regardless of the manner in which it is organized or governed or title to its property is held. Descriptive words, such as "a corporation" or "an unincorporated association", must not be included in the registration. Examples:

Shriners' Hospital for Crippled Children, St. Louis, Missouri, 12-3456789.

St. Mary's Roman Catholic Church, Albany, New York, 12-3456789.

Rodeph Shalom Sunday School, Philadelphia, Pennsylvania, 12-3456789.

(f) *States, public bodies and corporations, and public officers.* A bond may be registered in the name of a State, county, city, town, village, school district, or other political entity, public body, or corporation established by law (including a board, commission, administration, authority, or agency) which is the owner or official custodian of public funds, other than trust funds, or in the full legal title of the public officer having custody of the funds. Examples:

State of Maine.

Town of Rye, New York (Street Improvement Fund).

Maryland State Highway Administration.

Treasurer, City of Chicago.

(g) *The United States Treasury.* A person who desires to have a bond become the property of the United States upon his or her death may designate the United States Treasury as coowner or beneficiary. Examples:

George T. Jones 123-45-6789 or the United States Treasury.

George T. Jones 123-45-6789 P.O.D. the United States Treasury.

#### SUBPART C—LIMITATIONS ON ANNUAL PURCHASES

##### § 315.10 Limitations.

Specific limitations have been placed on the amounts of bonds of each series and savings notes that might be purchased in any one year in the name of any one person or organization. The amounts applicable to each series of bonds and savings notes for each specific year, which has varied from time to time, can be found in the appropriate offering circulars, as revised and amended.

##### § 315.11 Excess purchases.

The Commissioner of the Public Debt may permit excess purchases to stand in any particular case or class of cases.

#### SUBPART D—LIMITATIONS ON TRANSFER OR PLEDGE

##### § 315.15 Transfer.

Savings bonds are not transferable and are payable only to the owners named on the bonds, except as specifically provided in these regulations and then only in the manner and to the extent so provided.

##### § 315.16 Pledge.

(a) *General.* A savings bond may not be hypothecated, pledged, or used as security for the performance of an obligation, except as provided in paragraph (b) of this section.

(b) *Pledge under Treasury Circular No. 154.* A bond may be pledged by the registered owner in lieu of surety under the provisions of Department of the Treasury Circular No. 154, current revision (31 CFR, Part 225), if the bond approving officer is the Secretary of the Treasury. In this case, an irrevocable power of attorney shall be executed authorizing the Secretary of the Treasury to request payment.

#### SUBPART E—LIMITATIONS ON JUDICIAL PROCEEDINGS—NO STOPPAGE OR CAVEATS PERMITTED

##### § 315.20 General.

The following general rules apply to the recognition of a judicial determination on adverse claims affecting savings bonds:

(a) The Department of the Treasury will not recognize a judicial determination that gives effect to an attempted voluntary transfer inter vivos of a bond, or a judicial determination that impairs the rights of survivorship conferred by these regulations upon a coowner or beneficiary. All provisions of this Subpart are subject to these restrictions.

(b) The Department of the Treasury will recognize a claim against an owner of a savings bond and conflicting claims of ownership of, or interest in, a bond between coowners or between the registered owner and the beneficiary, if established by valid, judicial proceedings, but only as specifically provided in this Subpart. Section 315.23 specifies the evidence required to establish the validity of the judicial proceedings.

(c) The Department of the Treasury and the agencies that issue, reissue, or redeem savings bonds will not accept a notice of an adverse claim or notice of pending judicial proceedings, nor undertake to protect the interests of a litigant not in possession of a savings bond.

**§ 315.21 Payment to judgment creditors.**

(a) *Purchaser or officer under levy.* The Department of the Treasury will pay (but not reissue) a savings bond to the purchaser at a sale under a levy or to the officer authorized under appropriate process to levy upon property of the registered owner or coowner to satisfy a money judgment. Payment will be made only to the extent necessary to satisfy the money judgment. The amount paid is limited to the redemption value 60 days after the termination of the judicial proceedings. Payment of a bond registered in coownership form pursuant to a judgment or a levy against only one coowner is limited to the extent of that coowner's interest in the bond. That interest must be established by an agreement between the coowners or by a judgment, decree, or order of a court in a proceeding to which both coowners are parties.

(b) *Trustee in bankruptcy, receiver, or similar court officer.* The Department of the Treasury will pay, at current redemption value, a savings bond to a trustee in bankruptcy, a receiver of an insolvent's estate, a receiver in equity, or a similar court officer under the provisions of paragraph (a) of this section.

**§ 315.22 Payment or reissue pursuant to judgment.**

(a) *Divorce.* The Department of the Treasury will recognize a divorce decree that ratifies or confirms a property settlement agreement disposing of bonds or that otherwise settles the interests of the parties in a bond. Reissue of a savings bond may be made to eliminate the name of one spouse as owner, coowner, or beneficiary, or to substitute the name of one spouse for that of the other spouse as owner, coowner, or beneficiary pursuant to the decree. However, if the bond is registered in the name of one spouse with another person as coowner, there must be submitted either (1) a request for reissue by the other person or (2) a certified copy of a judgment, decree, or court order entered in proceedings to which the other person and the spouse named on the bond are parties, determining the extent of the interest of that spouse in the bond. Reissue will be permitted only to the extent of that spouse's interest. The evidence required under § 315.23 must be submitted in every case. When the divorce decree does not set out the terms of the property settlement agreement, a certified copy of the agreement must be submitted. Payment, rather than reissue, will be made if requested.

(b) *Gift causa mortis.* A savings bond belonging solely to one individual will be paid or reissued at the request of the person found by a court to be entitled by reason of a gift causa mortis from the sole owner.

(c) *Date for determining rights.* When payment or reissue under this section is to be made, the rights of the parties will be those existing under the regulations current at the time of the entry of the final judgment, decree, or court order.

**§ 315.23 Evidence.**

(a) *General.* To establish the validity of judicial proceedings, certified copies of the final judgment, decree, or court order, and of any necessary supplementary proceedings, must be submitted. If the judgment, decree, or court order was rendered more than six months prior to the presentation of the bond, there must also be submitted a certificate from the clerk of the court, under court seal, dated within six months of the presentation of the bond, showing that the judgment, decree, or court order is in full force.

(b) *Trustee in bankruptcy or receiver of an insolvent's estate.* A request for payment by a trustee in bankruptcy or a receiver of an insolvent's estate must be supported by appropriate evidence of appointment and qualification. The evidence must be certified by the clerk of the court, under court seal, as being in full force on a date that is not more than six months prior to the presentation of the bond.

(c) *Receiver in equity or similar court officer.* A request for payment by the receiver in equity or a similar court officer, other than a receiver of an insolvent's estate, must be supported by a copy of an order that authorizes the presentation of the bond for redemption, certified by the clerk of the court, under court seal, as being in full force on a date that is not more than six months prior to the presentation of the bond.



SUBPART F—RELIEF FOR LOSS, THEFT, DESTRUCTION, MUTILATION,  
DEFACEMENT, OR NONRECEIPT OF BONDS

**§ 315.25 General.**

Relief, by the issue of a substitute bond or by payment, is authorized for the loss, theft, destruction, mutilation, or defacement of a bond after receipt by the owner or his or her representative. As a condition for granting relief, the Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may require a bond of indemnity, in the form, and with the surety, or security, he considers necessary to protect the interests of the United States. In all cases the savings bond must be identified by serial number and the applicant must submit satisfactory evidence of the loss, theft, or destruction, or a satisfactory explanation of the mutilation or defacement.

**§ 315.26 Application for relief—after receipt of bond.**

(a) *Serial number known.* If the serial number of the lost, stolen, or destroyed bond is known, the claimant should execute an application for relief on the appropriate form and submit it to the Bureau of the Public Debt, Parkersburg, West Virginia 26101.

(b) *Serial number not known.* If the bond serial number is not known, the claimant must provide sufficient information to enable the Bureau of the Public Debt to identify the bond by serial number. See § 315.29(c). The Bureau will furnish the proper application form and instructions.

(c) *Defaced or mutilated bond.* A defaced bond and all available fragments of a mutilated bond should be submitted to the Bureau.

(d) *Execution of claims application.* The application must be made by the person or persons (including both coowners, if living) authorized under these regulations to request payment of the bonds. In addition—

(1) If the bond is in beneficiary form and the owner and beneficiary are both living, both will ordinarily be required to join in the application.

(2) If a minor named on a bond as owner, coowner, or beneficiary is not of sufficient competency and understanding to request payment, both parents will ordinarily be required to join in the application.

(e) If the application is approved, relief will be granted by the issuance of a bond bearing the same issue date as the bond for which the claim was filed or by the issuance of a check in payment.

**§ 315.27 Application for relief—nonreceipt of bond.**

If a bond issued on any transaction is not received, the issuing agent must be notified as promptly as possible and given all information available about the nonreceipt. An appropriate form and instructions will be provided. If the application is approved, relief will be granted by the issuance of a bond bearing the same issue date as the bond that was not received.

**§ 315.28 Recovery or receipt of bond before or after relief is granted.**

(a) *Recovery prior to granting relief.* If a bond reported lost, stolen, destroyed, or not received, is recovered or received before relief is granted, the Bureau of the Public Debt, Parkersburg, West Virginia 26101, must be notified promptly.

(b) *Recovery subsequent to granting of relief.* A bond for which relief has been granted is the property of the United States and, if recovered, must be promptly submitted to the Bureau of the Public Debt, Parkersburg, West Virginia 26101, for cancellation.

**§ 315.29 Adjudication of claims.**

(a) *General.* The Bureau of the Public Debt will adjudicate claims for lost, stolen or destroyed bonds on the basis of records created and regularly maintained in the ordinary course of business.

(b) *Claims filed ten years after payment.* A bond for which no claim has been filed within ten years of the recorded date of redemption will be presumed to have been properly paid. If a claim is subsequently filed, a photographic copy of the bond will not be available to support the disallowance. This provision will be effective 60 days

after the effective date of the Eleventh Revision of Department of the Treasury Circular No. 530 (31 CFR, Part 315).

(c) *Claims filed six years after final maturity.* No claim filed six years or more after the final maturity of a savings bond will be entertained, unless the claimant supplies the serial number of the bond.

## SUBPART G—INTEREST

### § 315.30 Series E bonds and savings notes.

Series E bonds and savings notes are discount securities. The accrued interest is added to the issue price at stated intervals and is payable only at redemption as part of the redemption value. All Series E bonds and savings notes have been extended and continue to earn interest until their final maturity dates, unless redeemed earlier. Information regarding extended maturity periods, investment yields and redemption values is found in Department of the Treasury Circular No. 653, current revision (31 CFR, Part 316) for Series E bonds, and in Department of The Treasury Circular, Public Debt Series No. 3-67, current revision (31 CFR, Part 342) for savings notes.

### § 315.31 Series H bonds.

(a) *General.* Series H bonds are current-income bonds issued at par (face amount). Interest on a Series H bond is paid semiannually by check, beginning six months from the issue date. All Series H bonds have been extended and continue to earn interest until their final maturity dates, unless redeemed earlier. If a bond is redeemed before its final maturity date, interest ceases as of the end of the interest payment period preceding redemption. For example, if a bond on which interest is payable on January 1 and July 1 is redeemed on September 1, interest ceases as of the preceding July 1, and no adjustment of interest will be made for the period from July 1 to September 1. However, if the date of redemption falls on an interest payment date, interest ceases on that date. Information regarding authorized extended maturity periods and investment yields is found in Department of the Treasury Circular No. 905, current revision (31 CFR, Part 332).

(b) *Payment of interest.* Series H bond interest accounts are maintained by the Bureau of the Public Debt, Parkersburg, West Virginia 26101. Interest will be paid on each interest payment date by check mailed to the address specified for the delivery of checks in the purchase application, exchange subscription, notification of change of address or request for reissue. If no instruction is given as to the delivery of interest checks, the address inscribed on the bond for the owner or the first-named coowner will be used.

(c) *Delivery of interest.*

(1) *Notices affecting delivery of interest checks.* To insure appropriate action, notices affecting the delivery of interest checks on Series H bonds, including changes of addresses, must be received by the Bureau of the Public Debt, Parkersburg, West Virginia 26101, at least one month prior to the interest payment date. Each notice must identify the bonds by the name and taxpayer identifying number of the bondowner. The notice must be signed by the owner or coowner, or, in the case of a minor or incompetent, as provided in paragraph (d) or (e) of this section.

(2) *Owner or coowner deceased.*

(i) *Sole owner.* Upon receipt of notice of the death of the owner of a bond, payment of interest on the bond will be suspended until satisfactory evidence is submitted as to who is authorized to endorse and collect interest checks on behalf of the estate of the decedent, in accordance with the provisions of Subpart L.

(ii) *Coowner.* Upon receipt of notice of the death of the coowner to whom interest is being mailed, payment of interest will be suspended until a request for change of address is received from the other coowner, if living, or, if not, until satisfactory evidence is submitted as to the individual who is authorized to endorse and collect interest checks on behalf of the estate of the last deceased coowner, in accordance with the provisions of Subpart L.

(iii) *Owner with beneficiary.* In the case of a bond registered in the form "A payable on death to B", the check will be drawn to the order of "A" alone unless the Bureau of the Public Debt, Parkersburg, West Virginia 26101, receives notice of A's death. In

that event, the payment of interest will be suspended until the bond is presented for payment or reissue. Interest so withheld will be paid to the person entitled to the bond.

(d) *Representative appointed for the estate of a minor, incompetent, absentee, et al.* Interest on Series H bonds is paid in accordance with the provisions of § 315.60 to the representative appointed for the estate of an owner who is a minor, incompetent, absentee, et al. If the registration of the bonds does not include a reference to the owner's status, the bonds should be submitted for reissue to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt, Parkersburg, West Virginia 26101, so that interest checks may be properly drawn and delivered. They must be accompanied by the proof of appointment required by § 315.60.

(e) *Adult incompetent's estate having no representative.* If an adult owner of a Series H bond is incompetent to endorse and collect the interest checks and no legal guardian or similar representative has been appointed to act for him or her, the relative, or other person, responsible for his or her care and support, may apply to the Bureau of the Public Debt for recognition as voluntary guardian for the purpose of receiving, endorsing, and collecting the checks.

(f) *Reissue during interest period.* Physical reissue of a Series H bond will be made without regard to interest payment dates. The Series H interest accounts maintained by the Bureau of the Public Debt will be closed in the first week of the month preceding each interest payment date. Interest checks will be drawn to the order of the persons shown to be entitled on these accounts as of the date the accounts are closed.

(g) *Endorsement of checks.* Interest checks must be endorsed in accordance with the regulations governing the endorsement and payment of Government warrants and checks, which are contained in Department of the Treasury Circular No. 21, current revision (31 CFR, Part 240).

(h) *Nonreceipt or loss of check.* If an interest check is not received or is lost after receipt, the Bureau of the Public Debt, Parkersburg, West Virginia 26101, should be notified and advised of the bond serial number, the inscription on the bond, including the taxpayer identifying number of the bondowner, and the interest payment date.

### § 315.32 Series A, B, C, D, F, G, J, and K bonds.

All bonds of these series have matured and no longer earn interest.

## SUBPART H—GENERAL PROVISIONS FOR PAYMENT

### § 315.35 Payment (redemption).

(a) *General.* Payment of a savings bond will be made to the person or persons entitled under the provisions of these regulations, except that checks in payment will not be delivered to addresses in areas with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States. See Department of the Treasury Circular No. 655, current revision (31 CFR, Part 211). Payment will be made without regard to any notice of adverse claims to a bond and no notification of stoppage or caveat against payment of a bond will be made.

(b) *Series A, B, C, D, F, and J.* A bond of Series A, B, C, D, F, or J will be paid at face value.

(c) *Series E and Savings Notes.* A Series E bond will be paid at any time after two months from issue date at the appropriate redemption value shown in Department of the Treasury Circular No. 653 (31 CFR, Part 316), current revision. A savings note will be paid at anytime at the appropriate redemption value shown in Department of the Treasury Circular, Public Debt Series No. 3-67, current revision (31 CFR, Part 342).

(d) *Series G and K.* A bond of Series G or K will be paid at face value plus the final semiannual interest due. For Series G bonds, the final interest paid with principal is \$1.25 per \$100; for Series K bonds, the final interest is \$6.90 per \$500.

(e) *Series H.* A Series H bond will be paid at face value at anytime after six months from issue date. However, a bond received for redemption during the calendar month preceding an interest payment date may not be redeemed until that date.



**§ 315.36 Payment during life of sole owner.**

A savings bond registered in single ownership form (i.e., without a coowner or beneficiary) will be paid to the owner during his or her lifetime upon surrender with an appropriate request.

**§ 315.37 Payment during lives of both coowners.**

A savings bond registered in coownership form will be paid to either coowner upon surrender with an appropriate request, and, upon payment (as determined in § 315.43), the other coowner will cease to have any interest in the bond. If both coowners request payment and payment is to be made by check, the check will be drawn in the form, "John A. Jones AND Mary C. Jones".

**§ 315.38 Payment during lifetime of owner of beneficiary bond.**

A savings bond registered in beneficiary form will be paid to the registered owner during his or her lifetime upon surrender with an appropriate request. Upon payment (as determined in § 315.43), the beneficiary will cease to have any interest in the bond.

**§ 315.39 Surrender for payment.**

(a) *Procedure for bonds of Series A to E, inclusive, in the names of individual owners or coowners only.* An individual who is the owner or coowner of a bond of Series A, B, C, D, or E may present the bond to an authorized paying agent for redemption. The presenter must be prepared to establish his or her identity in accordance with Treasury instructions and identification guidelines. The owner or coowner must sign the request for payment on the bond or, if authorized, on a separate detached request, and add his or her address. In addition, in the case of a Series E bond or savings note, the presenter must record his or her social security number on the face of the security, provided it does not already appear in the inscription. Paying agents are authorized to refuse payment in any case where the presenter's number is not provided. If the request for payment has been signed, or signed and certified, before presentation of the bond, the paying agent must be satisfied that the person presenting the bond for payment is the owner or coowner and may require the person to sign the request for payment again. If the bond is in order for payment, the paying agent will make immediate payment at the current redemption value without charge to the presenter. Paying agents are not authorized to process any case involving partial redemption or any case in which supporting evidence is required.

(b) *Procedure for all other cases.* In the case of a bond to which the procedure in paragraph (a) of this section does not apply, or if otherwise preferred, the owner or coowner, or other person entitled to payment, should appear before an officer authorized to certify requests for payment, establish his or her identity, sign the request for payment, and provide information as to the address to which the check in payment is to be mailed. In addition, in the case of a Series E bond or savings note, the presenter must record his or her social security number on the face of the security, provided it does not already appear in the inscription. The bond must be forwarded to a Federal Reserve Bank or Branch or the Bureau of the Public Debt. Usually, payment will be expedited by submission to a Federal Reserve Bank or Branch. In all cases, the cost and risk of presentation of a bond will be borne by the owner. Payment will be made by check drawn to the order of the registered owner or other person entitled and will be mailed to the address requested.

(c) *Date of request.* Requests executed more than six months before the date of receipt of a bond for payment will not be accepted. Neither will a bond be accepted if payment is requested as of a date more than three months in the future.

**§ 315.40 Special provisions for payment.**

(a) *Owner's signature not required.* A bond may be paid by a paying agent or Federal Reserve Bank without the owner's signature to the request for payment, if the bond bears the special endorsement of a financial institution specifically qualified to place such an endorsement on savings bonds under the provisions of Department of the Treasury Circular No. 888, current revision (31 CFR, Part 330).

(b) *Signature by mark.* A signature by mark (X) must be witnessed by at least one disinterested person and a certifying officer. See Subpart J. The witness must attest to the signature by mark substantially as follows: "Witness to signature by mark," followed by his or her signature and address.

(c) *Name change.* If the name of the owner, coowner, or other person entitled to payment, as it appears in the registration or in evidence on file in the Bureau of the Public Debt, has been changed in any legal manner, the signature to the request for payment must show both names and the manner in which the change was made; for example, "Mary T. Jones Smith (Mary T. J. Smith or Mary T. Smith) changed by marriage from Mary T. Jones," or "John R. Young, changed by order of court from Hans R. Jung," See § 315.50.

(d) *Attorneys-in-fact.* A request for payment signed by an attorney-in-fact will be recognized if it is accompanied by a copy of a power of attorney, executed before a certifying officer, that authorizes the attorney-in-fact to sell or cash the grantor's Treasury securities. See Sec. 315.65 for separate rules relating to the use of powers of attorney for incompetent or physically disabled individuals.

#### § 315.41 Partial redemption.

A bond of any series may be redeemed in part at current redemption value, but only in an amount corresponding to one or more authorized denominations, upon surrender of the bond to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt in accordance with § 315.39(b). In any case in which partial redemption is requested, the phrase "to the extent of \$\_\_\_ (face amount) and reissue of the remainder" should be added to the request. Upon partial redemption of the bond, the remainder will be reissued as of the original issue date, as provided in Subpart I.

#### § 315.42 Nonreceipt or loss of check issued in payment.

If a Treasury check in payment of a bond surrendered for redemption is not received within a reasonable time or is lost after receipt, notice should be given to the same agency to which the bond was surrendered for payment. The notice should give the date the bond was surrendered for payment, and describe the bond by series, denomination, serial number, and registration, including the taxpayer identifying number of the owner.

#### § 315.43 Effective date of request for payment.

The Department of the Treasury will treat the receipt of a bond with an appropriate request for payment by (a) a Federal Reserve Bank or Branch, (b) the Bureau of the Public Debt, or (c) a paying agent authorized to pay that bond, as the date upon which the rights of the parties are fixed for the purpose of payment.

#### § 315.44 Withdrawal of request for payment.

(a) *Withdrawal by owner or coowner.* An owner or coowner, who has surrendered a bond to a Federal Reserve Bank or Branch or to the Bureau of the Public Debt or an authorized paying agent with an appropriate request for payment, may withdraw the request if notice of intent to withdraw is received by the same agency prior to payment either in cash or through the issuance of the redemption check.

(b) *Withdrawal on behalf of deceased owner or incompetent.* A request for payment may be withdrawn under the same conditions as in paragraph (a) of this section by the executor or administrator of the estate of a deceased owner or by the person or persons who would have been entitled to the bond under Subpart L, or by the legal representative of the estate of a person under legal disability, unless surrender of the bond for payment has eliminated the interest of a surviving coowner or beneficiary. See § 315.70(b) and (c).

### SUBPART I—REISSUE AND DENOMINATIONAL EXCHANGE

#### § 315.45 General.

Reissue of a bond may be made only under the conditions specified in these regulations, and only at (a) a Federal Reserve Bank or Branch, or (b) the Bureau of the

Public Debt. Reissue will not be made if the request is received less than one full calendar month before the final maturity date of a bond. The request, however, will be effective to establish ownership as though the reissue had been made.

#### § 315.46 Effective date of request for reissue.

The Department of the Treasury will treat the receipt by (a) a Federal Reserve Bank or Branch or (b) the Bureau of the Public Debt of a bond and an acceptable request for reissue as determining the date upon which the rights of the parties are fixed for the purpose of reissue. For example, if the owner or either coowner of a bond dies after the bond has been surrendered for reissue, the bond will be regarded as having been reissued in the decedent's lifetime.

#### § 315.47 Authorized reissue—during lifetime.

A bond belonging to an individual may be reissued in any authorized form of registration upon an appropriate request for the purposes outlined below:

(a) *Single ownership.* A bond registered in single ownership form may be reissued—

(1) To add a coowner or beneficiary;

(2) To name a new owner, with or without a coowner or beneficiary, but only if (i) the new owner is related to the previous owner by blood (including legal adoption) or marriage, (ii) the previous owner and the new owner are parties to a divorce or annulment, or (iii) the new sole owner is the trustee of a personal trust estate which was created by the previous owner or which designates as beneficiary either the previous owner or a person related to him or her by blood (including legal adoption) or marriage.

(b) *Coownership.*

(1) *Reissue—to name a related individual as owner or coowner.* During the lifetime of both coowners, a coownership bond may be reissued in the name of another individual related by blood (including legal adoption) or marriage to either coowner—

(i) As single owner,

(ii) As owner with one of the original coowners as beneficiary, or

(iii) As a new coowner with one of the original coowners.

(2) *Reissue—to name either coowner alone or with another individual as coowner or beneficiary.* During the lifetime of both coowners, a coownership bond may be reissued in the name of either coowner alone or with another individual as coowner or beneficiary if—

(i) After issue of the submitted bond, either coowner named thereon marries, or the coowners are divorced or legally separated from each other, or their marriage is annulled; or

(ii) Both coowners on the submitted bond are related by blood (including legal adoption) or marriage to each other.

(3) *Reissue—to name the trustee of a personal trust estate.* A bond registered in coownership form may be reissued to name a trustee of a personal trust estate created by either coowner or by some other person if (i) either coowner is a beneficiary of the trust, or (ii) a beneficiary of the trust is related by blood or marriage to either coowner.

(c) *Beneficiary.* A bond registered in beneficiary form may be reissued—

(1) To name the beneficiary as coowner;

(2) To eliminate the name of the owner and to name as owner a custodian for the beneficiary, if a minor, under a statute authorizing gifts to minors;

(3) To eliminate the beneficiary or to substitute another individual as beneficiary, but only if the request is supported by the certified consent of the beneficiary or by proof of his or her death; or

(4) To eliminate the names of the owner and the beneficiary and to name as new owner the trustee of the personal trust estate which was created by the previous owner or which designates as beneficiary either the previous owner or a person related to him or her by blood (including legal adoption) or marriage, but only if the request is supported by the certified consent of the beneficiary or by proof of his or her death.



### § 315.48 Restrictions on reissue.

(a) *Denominational exchange.* Reissue is not permitted solely to change denominations.

(b) *United States Treasury.* Reissue may not be made to eliminate the United States Treasury as coowner or beneficiary.

### § 315.49 Correction of errors.

A bond may be reissued to correct an error in registration upon appropriate request, supported by satisfactory proof of the error.

### § 315.50 Change of name.

An owner, coowner, or beneficiary whose name is changed by marriage, divorce, annulment, order of court, or in any other legal manner after the issue of bond should submit the bond with a request for reissue to substitute the new name for the name inscribed on the bond. Documentary evidence may be required in any appropriate case.

### § 315.51 Requests for reissue.

A request for reissue of bonds in coownership form during the lifetime of the coowners must be signed by both coowners, except that a request solely to eliminate the name of one coowner may be signed by that coowner only. A bond registered in beneficiary form may be reissued upon the request of the owner, supported by the certified consent of the beneficiary or by proof of his or her death. Public Debt forms are available for requesting reissue.

## SUBPART J—CERTIFYING OFFICERS

### § 315.55 Individuals authorized to certify.

The following individuals are authorized to act as certifying officers for the purpose of certifying a request for payment, reissue, or a signature to a Public Debt form:

(a) *Officers generally authorized.*

(1) *At banks, trust companies, and member organizations of the Federal Home Loan Bank System.*

(i) Any officer of a bank incorporated in the United States, the territories or possessions of the United States, or the Commonwealth of Puerto Rico.

(ii) Any officer of a trust company incorporated in the United States, the territories or possessions of the United States, or the Commonwealth of Puerto Rico.

(iii) Any officer of an organization that is a member of the Federal Home Loan Bank System. This includes Federal savings and loan associations.

(iv) Any officer of a foreign branch or a domestic branch of an institution described in paragraphs (a)(1) (i) through (iii) of this section.

(v) Any officer of a Federal Reserve Bank, a Federal Land Bank, or a Federal Home Loan Bank.

(vi) Any employee of an institution described in paragraph (a)(1) (i) through (v) of this section, who is expressly authorized to certify by the institution. Certification by these officers or designated employees must be authenticated by a legible imprint either of a corporate stamp of the institution or of the issuing or paying agent's stamp. An employee authorized to certify requests must sign his or her name over the title "Designated Employee".

(2) *At issuing agents that are not banks or trust companies.* Any officer of an organization, not a bank or a trust company, that is qualified as an issuing agent for savings bonds. The agent's stamp must be imprinted in the certification.

(3) *By United States officials.* Any judge, clerk, or deputy clerk of a United States court, including United States courts for the territories and possessions of the United States, and the Commonwealth of Puerto Rico or any United States Commissioner or United States Attorney.

(b) *Officers with limited authority.*

(1) *In the Armed Forces.* Any commissioned officer or warrant officer of the Armed Forces of the United States, but only for members of the respective services, their

families, and civilian employees at posts, bases, or stations. The certifying officer must indicate his or her rank and state that the individual signing the request is one of the class whose request the certifying officer is authorized to certify.

(2) *At Veterans Administration facilities, Federal penal institutions, and United States Public Health Service hospitals.* Any officer in charge of a home, hospital, or other facility of the Veterans Administration, but only for the patients, or employees of the facility; any officer of a Federal penal institution or a United States Public Health Service hospital expressly authorized to certify by the Secretary of the Treasury or his designee, but only for the inmates, patients or employees of the institution involved. Officers of Veterans Administration facilities, Federal penal institutions, and Public Health Service hospitals must use the stamp of the particular institution or service.

(c) *Authorized officers in foreign countries.* Any United States diplomatic or consular representative, or the officer of a foreign branch of a bank or trust company incorporated in the United States whose signature is attested by an imprint of the corporate stamp or is certified to the Department of the Treasury. If none of these individuals is available, a notary public or other officer authorized to administer oaths may certify, but his or her official character and jurisdiction must be certified by a United States diplomatic or consular officer under seal of his or her office.

(d) *Authorized officers in particular localities.* The Governor and the Treasurer of Puerto Rico; the Governor and the Commissioner of Finance of the Virgin Islands; the Governor and the Director of Finance of Guam; and the Governor and the Director of Administrative Services of American Samoa; and designated officers of the Panama Canal Commission.

(e) *Special provisions.* If no certifying officer is readily accessible, the Commissioner of the Public Debt, Deputy Commissioner, any Assistant Commissioner, or other designated official of the Bureau or of a Federal Reserve Bank or Branch is authorized to make special provision for any particular case.

#### § 315.56 General instructions and liability.

(a) *Certification procedure.* Certifying officers at financial institutions qualified as paying agents should observe the Treasury's payment instructions and identification guidelines in certifying savings bonds and savings notes being forwarded to a Federal Reserve Bank for any transaction. Other certifying officers should provide certification services for persons with whom they have substantial personal acquaintance, and for other persons whose identities have been unmistakably established. A notation showing exactly how identification was established should be placed on the back of the security or Public Debt form, or in a separate record. As part of the certification, the certifying officer must affix his or her official signature, title and address, the exact date of execution and, where one is available, a corporate stamp or issuing or paying agent's stamp.

(b) *Liability.* The certifying officer and, if such person is an officer or an employee of an organization, the organization will be held fully responsible for the adequacy of the identification.

#### § 315.57 When a certifying officer may not certify.

Certifying officers may not certify the requests for payment of bonds, or appropriate Public Debt forms if, in their own right or in a representative capacity, they

- (a) Have an interest in the bonds, or
- (b) Will, by virtue of the requests being certified, acquire an interest in the bonds.

#### § 315.58 Forms to be certified.

When required in the instructions on a Public Debt form, the form must be signed before an authorized certifying officer.

SUBPART K—MINORS, INCOMPETENTS, AGED PERSONS, ABSENTEES, ET AL.

#### § 315.60 Conditions for payment to representative of an estate.

(a) *General.* The representative of an estate of an owner who is a minor, an aged person, incompetent, absentee, et al., may receive upon request—

- (1) If the registration shows the name and capacity of the representative;
  - (2) If the registration shows the capacity but not the name of the representative and the request is accompanied by appropriate evidence; or
  - (3) If the registration includes neither the name of the representative nor his or her capacity by the request is accompanied by appropriate evidence.
- (b) *Evidence.* Appropriate evidence for paragraphs (a)(2) and (a)(3) of this section includes a certified copy of the letters of appointment or, if the representative is not appointed by a court, other proof of qualification. Except in the case of corporate fiduciaries, the evidence must show that the appointment is in full force and be dated not more than one year prior to the presentation of the bond for payment. The request for payment appearing on the back of a bond must be signed by the representative as such, for example, "John S. Jones, guardian (committee) of the estate of Henry W. Smith, a minor (an incompetent)."

#### § 315.61 Payment after death.

After the death of the ward, and at any time prior to the representative's discharge, the representative of the estate will be entitled to obtain payment of a bond to which the ward was solely entitled.

#### § 315.62 Payment to minors.

If the owner of a savings bond is a minor and the form of registration does not indicate that there is a representative of the minor's estate, payment will be made to the minor upon his or her request, provided the minor is of sufficient competency to sign the request for payment and to understand the nature of the transaction. In general, the fact that the request for payment has been signed by a minor and certified will be accepted as sufficient proof of competency and understanding.

#### § 315.63 Payment to a parent or other person on behalf of a minor.

If the owner of a savings bond is a minor and the form of registration does not indicate that there is a representative of his or her estate, and if the minor is not of sufficient competency to sign the request for payment and to understand the nature of the transaction, payment will be made to either parent with whom the minor resides or to whom legal custody has been granted. If the minor does not reside with either parent, payment will be made to the person who furnishes the chief support for the minor. The request must appear on the back of the bond in one of the following forms:

##### (a) *Request by parent.*

I certify that I am the mother of John C. Jones (with whom he resides) (to whom legal custody has been granted). He is—years of age and is not of sufficient understanding to make this request.

Mary Jones on behalf of John C. Jones.

##### (b) *Request by other person.*

I certify that John C. Jones does not reside with either parent and that I furnish his chief support. He is— years of age and is not of sufficient understanding to make this request.

Alice Brown, grandmother, on behalf of John C. Jones.

#### § 315.64 Payment, reinvestment, or exchange—voluntary guardian of an incompetent.

When an adult owner of bonds is incapable of requesting payment and there is no other person legally qualified to do so, the relative or other person responsible for the owner's care and support may submit an application for recognition as voluntary guardian for the purpose of redeeming the bonds in the following situations:

(a) The proceeds of the bonds are needed to pay expenses already incurred, or to be incurred during any 90-day period, for the support of the incompetent or his or her legal dependents.

(b) If the bonds have finally matured and it is desired to redeem them and reinvest the proceeds in other savings bonds, the new bonds must be registered in the name of the incompetent, followed by words showing he or she is under voluntary guardianship; for example, "John Jones 123-45-6789, under voluntary guardianship". A living coowner or beneficiary named on the matured bonds must be designated on the new bonds unless the named person furnishes a certified statement consenting to



omission of his or her name. If an amount insufficient to purchase an additional bond of any authorized denomination of either series remains after the reinvestment, the voluntary guardian may furnish additional funds sufficient to purchase another bond of either series in the lowest available denomination. If additional funds are not furnished, the remaining amount will be paid to the voluntary guardian for the use and benefit of the incompetent. The provisions for reinvestment of the proceeds of matured bonds are equally applicable to any authorized exchange of bonds of one series for those of another.

**§ 315.65 Payment—attorney-in-fact of an incompetent or a physically disabled person.**

A request for payment by an individual as attorney-in-fact of an incompetent or a physically disabled owner will be honored if the power of attorney grants the attorney-in-fact authority to sell or cash the grantor's securities, sell his or her personal property, or otherwise grants similar authority. In the case of incompetency or total incapacity, the power of attorney must provide that the grantor's subsequent disability will not affect the authority granted. The request must be supported in all cases by a copy of the power of attorney and medical evidence of the grantor's condition.

**§ 315.66 Reissue.**

A bond on which a minor or other person under legal disability is named as the owner or coowner, or in which he or she has an interest, may be reissued under the following conditions:

(a) A minor for whose estate no representative has been appointed may request reissue if the minor is of sufficient competency to sign his or her name to the request and to understand the nature of the transaction.

(b) A bond on which a minor is named as beneficiary or coowner may be reissued in the name of a custodian for the minor under a statute authorizing gifts to minors upon the request of the adult whose name appears on the bond as owner or coowner.

(c) A minor coowner for whose estate no representative has been appointed, may be named sole owner upon the request of the competent coowner.

(d) Reissue to eliminate the name of a minor or incompetent for whose estate a legal representative has been appointed is permitted only if supported by evidence that a court has authorized the representative of the minor's or incompetent's estate to request the reissue. See § 315.23.

Except to the extent provided in paragraphs (a) through (d), above, reissue will be restricted to a form of registration which does not adversely affect the existing ownership or interest of a minor who is not of sufficient understanding to make a request, or other person under legal disability. Requests for reissue should be executed by the person authorized to request payment under § 315.60 and § 315.63, or the person who may request recognition as voluntary guardian under § 315.64.

**SUBPART L—DECEASED OWNER, COOWNER OR BENEFICIARY**

**§ 315.70 General rules governing entitlement.**

The following rules govern ownership or entitlement where one or both of the persons named on a bond have died without the bond having been surrendered for payment or reissue:

(a) *Single owner bond.* If the owner of a bond registered in single ownership form has died, the bond becomes the property of that decedent's estate, and payment or reissue will be made as provided in this Subpart.

(b) *Coowner bond.*

(1) *One coowner deceased.* If one of the coowners named on a bond has died, the surviving coowner will be recognized as its sole and absolute owner, and payment or reissue will be made as though the bond were registered in the name of the survivor alone. Any request for reissue by the surviving coowner must be supported by proof of death of the other coowner.

(2) *Both coowners deceased.* If both coowners named on a bond have died, the bond becomes the property of the estate of the coowner who died last, and payment or reissue will be made as if the bond were registered in the name of the last deceased

coowner alone. Proof of death of both coowners will be required to establish the order of death.

(3) *Simultaneous death of both coowners.* If both coowners die under conditions where it cannot be established, either by presumption of law or otherwise, which coowner died first, the bond becomes the property of both equally, and payment or reissue will be made accordingly.

(c) *Beneficiary bond.*

(1) *Owner deceased.* If the owner of a bond registered in beneficiary form has died and is survived by the beneficiary, upon proof of death of the owner, the beneficiary will be recognized as the sole and absolute owner of the bond. Payment or reissue will be made as though the bond were registered in the survivor's name alone. A request for payment or reissue by the beneficiary must be supported by proof of death of the owner.

(2) *Beneficiary deceased.* If the beneficiary's death occurs before, or simultaneous with, that of the registered owner, payment or reissue will be made as though the bond were registered in the owner's name alone. Proof of death of the owner and beneficiary is required to establish the order of death.

(d) *Nonresident aliens.* If the person who becomes entitled to a bond because of the death of an owner is an alien who is a resident of an area with respect to which the Department of the Treasury restricts or regulates the delivery of checks drawn against funds of the United States or its agencies or instrumentalities, delivery of the redemption check will not be made so long as the restriction applies. See Department of the Treasury Circular No. 655, current revision (31 CFR, Part 211).

### § 315.71 Estate administered.

(a) *During administration.* The legal representative of an estate may request payment of bonds, including interest or redemption checks, belonging to the estate or may have the bonds reissued in the names of the persons entitled to share in the estate under the following conditions:

(1) When there is more than one legal representative, all must join in the request for payment or reissue, unless § 315.75(a)(1) or (b) applies.

(2) The request for payment or reissue must be signed in the form: "John A. Jones, administrator of the estate (or executor of the will) of Henry M. Jones, deceased". The request must be supported by evidence of the legal representative's authority in the form of a court certificate or a certified copy of the legal representative's letters of appointment which must be dated within six months of the date of presentation of the bond, unless the evidence shows that the appointment was made within one year prior to the presentation of the bond.

(3) For reissue, the legal representative must certify that each person in whose name reissue is requested is entitled to the extent specified and must certify that each person has consented to the reissue. If a person in whose name reissue is requested desires to name a coowner or beneficiary, the person must execute an additional request for reissue on the appropriate form.

(b) *After administration.* If the estate of the decedent has been settled through judicial proceedings, the bond and interest and redemption checks will be paid, or the bond will be reissued, upon the request of the person shown to be entitled by the court order. The request must be supported by a certified copy of the legal representative's court-approved final account, the decree of distribution, or other pertinent court records. If two or more persons have an interest in the bond, they must enter into an agreement concerning the bond's disposition. If the person entitled desires to name a coowner or beneficiary, a separate request must be made on an appropriate form.

(c) *Special provisions for small amounts.* Special procedures are available for establishing entitlement to, or effecting disposition of, savings bonds and interest and redemption checks if the aggregate face amount, excluding interest checks, does not exceed \$1,000.

### § 315.72 Estate not administered.

(a) *Special State law provisions.* A request for payment or reissue of a bond by the person who has qualified under State law to receive or distribute the assets of a

decedent's estate will be accepted; provided evidence of the person's authority is submitted.

(b) *Agreement of persons entitled.* If there is no legal representative for the estate of a decedent, the bonds will be paid to, or reissued in the name of, the persons entitled, pursuant to an agreement and request executed by all persons entitled to share in the decedent's personal estate. If the persons entitled to share in the decedent's personal estate include minors or incompetents, payment or reissue of the bonds must be made to them or in their names unless their interest in the bonds is otherwise protected.

(c) *Creditors.* An institutional creditor of a deceased owner's estate is entitled to payment only to the extent of its claim.

(d) *Special provisions for payment of small amounts—survivors of the decedent.*

(1) If the face amount of the bond does not exceed \$500 and there is no legal representative of the deceased owner's estate, the bond will be paid upon the request of the person who paid the burial expenses and who has not been reimbursed.

(2) If there is no legal representative of the estate of a decedent who died without a will, and the total face amount of bonds in the estate does not exceed \$1,000 (face amount), the bonds may be paid to the decedent's survivors upon request in the following order of precedence:

- (i) Surviving spouse;
- (ii) If no surviving spouse, to the child or children of the decedent, and the descendants of deceased children by representation;
- (iii) If none of the above, to the parents of the decedent, or the survivor;
- (iv) If none of the above, to the brothers and sisters, and the descendants of deceased brothers or sisters by representation;
- (v) If none of the above, to other next-of-kin, as determined by the laws of the owner's domicile at death;
- (vi) If none of the above, to persons related to the decedent by marriage.

The payment pursuant to this subsection shall be made upon the request and agreement of the survivors to receive the redemption proceeds individually and for the account of any persons entitled. Interest checks held for the estate of a decedent will be distributed with the bonds.

## SUBPART M—FIDUCIARIES

### § 315.75 Payment or reissue during the existence of the fiduciary estate.

(a) *Payment or reissue before maturity.* (1) *Request from the fiduciary named in the registration.* A request for reissue or payment prior to maturity must be signed by all of the fiduciaries unless by statute, decree of court, or the terms of the governing instrument, any lesser number may properly execute the request. If the fiduciaries named in the registration are still acting, no further evidence will be required. In other cases, evidence to support the request will be required, as specified:

(i) *Fiduciaries by title only.* If the bond is registered only in the titles, without the names, of fiduciaries not acting as a board, satisfactory evidence of their incumbency must be furnished, except in the case of bonds registered in the title of public officers as trustees.

(ii) *Boards, committees, commissions, etc.* If a bond is registered in the name of a governing body which is empowered to act as a unit, and which holds title to the property of a religious, educational, charitable or nonprofit organization or a public corporation, the request should be signed in the name of the body by an authorized person. Ordinarily, a signed and certified request will be accepted without further evidence.

(iii) *Corporate fiduciaries.* If a bond is registered in the name of a public or private corporation or a governmental body as fiduciary, the request must be signed by an authorized officer in the name of the organization as fiduciary. Ordinarily, a signed and certified request will be accepted without further evidence.

(2) *Trustee of a common trust fund.* A bond held by a financial institution in a fiduciary capacity may be reissued in the name of the institution as trustee of its common trust fund to the extent that participation in the common trust fund is



authorized by law or regulation. The request for reissue should be executed by the institution and any cofiduciary.

(3) *Successor fiduciary.* If the fiduciary in whose name the bond is registered has been replaced by another fiduciary, satisfactory evidence of successorship must be furnished.

(b) *Payment at or after final maturity.* At or after final maturity, a request for payment signed by any one or more of the fiduciaries will be accepted. Payment will be made by check drawn as the bond is registered.

#### **§ 315.76 Payment or reissue after termination of the fiduciary estate.**

A bond registered in the name or title of a fiduciary may be paid or reissued to the person who has become entitled by reason of the termination of a fiduciary estate. Requests for reissue made by a fiduciary pursuant to the termination of a fiduciary estate should be made on the appropriate form. Requests for payment or reissue by other than the fiduciary must be accompanied by evidence to show that the person has become entitled in accordance with applicable State law or otherwise. When two or more persons have become entitled, the request for payment or reissue must be signed by each of them.

#### **§ 315.77 Exchange by fiduciaries.**

Fiduciaries are authorized to request an exchange of bonds of one series for those of another, pursuant to any applicable Department of the Treasury offering. A living coowner or beneficiary named on the bonds submitted in exchange may be retained in the same capacity on the new bonds.

### **SUBPART N—PRIVATE ORGANIZATIONS (CORPORATIONS, ASSOCIATIONS, PARTNERSHIPS, ETC.) AND GOVERNMENTAL AGENCIES, UNITS AND OFFICERS**

#### **§ 315.80 Payment to corporations or unincorporated associations.**

A bond registered in the name of a private corporation or an unincorporated association will be paid to the corporation or unincorporated association upon a request for payment on its behalf by an authorized officer. The signature to the request should be in the form, for example, "The Jones Coal Company, a corporation, by John Jones, President", or "The Lotus Club, an unincorporated association, by William A. Smith, Treasurer". A request for payment so signed and certified will ordinarily be accepted without further evidence of the officer's authority.

#### **§ 315.81 Payment to partnerships.**

A bond registered in the name of an existing partnership will be paid upon a request for payment signed by a general partner. The signature to the request should be in the form, for example, "Smith and Jones, a partnership, by John Jones, a general partner". A request for payment so signed and certified will ordinarily be accepted as sufficient evidence that the partnership is still in existence and that the person signing the request is authorized.

#### **§ 315.82 Reissue or payment to successors of corporations, unincorporated associations, or partnerships.**

A bond registered in the name of a private corporation, an unincorporated association, or a partnership which has been succeeded by another corporation, unincorporated association, or partnership by operation of law or otherwise, in any manner whereby the business or activities of the original organization are continued without substantial change, will be paid to or reissued in the name of the succeeding organization upon appropriate request on its behalf, supported by satisfactory evidence of successorship. The appropriate form should be used.

#### **§ 315.83 Reissue or payment on dissolution of corporation or partnership.**

(a) *Corporations.* A bond registered in the name of a private corporation which is in the process of dissolution will be paid to the authorized representative of the corporation upon a request for payment, supported by satisfactory evidence of the

representative's authority. At the termination of dissolution proceedings, the bond may be reissued upon the request of the authorized representative in the names of those persons, other than creditors, entitled to the assets of the corporation, to the extent of their respective interests. Proof will be required that all statutory provisions governing the dissolution of the corporation have been complied with and that the persons in whose names reissue is requested are entitled and have agreed to the reissue. If the dissolution proceedings are under the direction of a court, a certified copy of an order of the court, showing the authority of the representative to make the distribution requested must be furnished.

(b) *Partnerships.* A bond registered in the name of a partnership which has been dissolved by death or withdrawal of a partner, or in any other manner—

(1) will be paid upon a request for payment by any partner or partners authorized by law to act on behalf of the dissolved partnership, or

(2) will be paid to or reissued in the names of the persons entitled as the result of such dissolution to the extent of their respective interests, except that reissue will not be made in the names of creditors. The request must be supported by satisfactory evidence of entitlement, including proof that the debts of the partnership have been paid or properly provided for. The appropriate form should be used.

#### **§ 315.84 Payment to certain institutions.**

A bond registered in the name of a church, hospital, home, school, or similar institution, without reference in the registration to the manner in which it is organized or governed or to the manner in which title to its property is held, will be paid upon a request for payment signed on behalf of such institution by an authorized representative. A request for payment signed by a pastor of a church, superintendent of a hospital, president of a college, or by any official generally recognized as having authority to conduct the financial affairs of the particular institution will ordinarily be accepted without further proof of authority. The signature to the request should be in the form, for example, "Shriners' Hospital for Crippled Children, St. Louis, Missouri, by William A. Smith, Superintendent", or "St. Mary's Roman Catholic Church, Albany, New York, by the Rev. John Smyth, Pastor".

#### **§ 315.85 Reissue in name of trustee or agent for reinvestment purposes.**

A bond registered in the name of a religious, educational, charitable or nonprofit organization, whether or not incorporated, may be reissued in the name of a financial institution, or an individual, as trustee or agent. There must be an agreement between the organization and the trustee or agent holding funds of the organization, in whole or in part, for the purpose of investing and reinvesting the principal and paying the income to the organization. Reissue should be requested on behalf of the organization by an authorized officer using the appropriate form.

#### **§ 315.86 Reissue upon termination of investment agency.**

A bond registered in the name of a financial institution, or individual, as agent for investment purposes only, under an agreement with a religious, an educational, a charitable, or a nonprofit organization, may be reissued in the name of the organization upon termination of the agency. The former agent should request such reissue and should certify that the organization is entitled by reason of the termination of the agency. If such request and certification are not obtainable, the bond will be reissued in the name of the organization upon its own request, supported by satisfactory evidence of the termination of the agency. The appropriate form should be used.

#### **§ 315.87 Payment to governmental agencies, units, or their officers.**

(a) *Agencies and units.* A bond registered in the name of a State, county, city, town, village, or in the name of a Federal, State, or local governmental agency, such as a board, commission, or corporation, will be paid upon a request signed in the name of the governmental agency or unit by an authorized officer. A request for payment so signed and certified will ordinarily be accepted without further proof of the officer's authority.

(b) *Officers.* A bond registered in the official title of an officer of a governmental agency or unit will be paid upon a request for payment signed by the officer. The

request for payment so signed and certified will ordinarily be accepted as proof that the person signing is the incumbent of the office.

#### SUBPART O—MISCELLANEOUS PROVISIONS

##### § 315.90 Waiver of regulations.

The Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may waive or modify any provision or provisions of these regulations. He may do so in any particular case or class of cases for the convenience of the United States or in order to relieve any person or persons of unnecessary hardship, (a) if such action would not be inconsistent with law or equity, (b) if it does not impair any existing rights, and (c) if he is satisfied that such action would not subject the United States to any substantial expense or liability.

##### § 315.91 Additional requirements; bond of indemnity.

The Commissioner of the Public Debt, as designee of the Secretary of the Treasury, may require (a) such additional evidence as he may consider necessary or advisable, or (b) a bond of indemnity, with or without surety, in any case in which he may consider such a bond necessary for the protection of the interests of the United States.

##### § 315.92 Preservation of rights.

Nothing contained in these regulations shall be construed to limit or restrict existing rights which holders of savings bonds previously issued may have acquired under circulars offering the bonds for sale or under the regulations in force at the time of the purchase.

##### § 315.93 Supplements, amendments, or revisions.

The Secretary of the Treasury may at any time, or from time to time, prescribe additional, supplemental, amendatory, or revised rules and regulations governing the United States Savings Bonds and Savings Notes to which this circular applies.

PAUL H. TAYLOR,  
*Fiscal Assistant Secretary.*

### Domestic Finance

#### **Exhibit 18.—Statement of Assistant Secretary Altman, October 22, 1979, before the Subcommittee on Economic Stabilization of the House Committee on Banking, Finance and Urban Affairs, on Federal credit programs**

I welcome this opportunity to discuss H.R. 3905, the National Alcohols and Alcohol Fuel and Farm Commodity Production Act of 1979, as reported by the House Agriculture Committee. I will comment on the new Federal credit program which would be created by section 2 of the bill. The subcommittee has specifically requested the Department's assessment of any possible inflationary or anti-inflationary effects of the bill.

The total volume of credit in our economy at any time is limited by a number of constraints, including the constraints of monetary policy and the level of interest rates. Federal credit programs have the effect of changing the allocation of these limited credit resources by lowering the cost of credit to preferred borrowers. Indeed, that is their purpose. Federal credit programs reflect determinations by Congress that the credit markets, in their normal functioning, do not supply the amount of credit deemed desirable to the class of borrowers made eligible for assistance under the program. Yet, given a limited supply of credit available to the economy, the increased demands of Federal credit programs add to the pressures on interest rates, tending to raise interest costs for all borrowers including the Federal Government. For these reasons, proposals to create new Federal credit programs or to expand existing programs should be carefully scrutinized.



Let me turn now to the importance of the structure of a Federal credit program. The existence of a Federal credit program will generate a demand for it, whether it is needed or not. Thus, it is important that a Federal credit program be structured to minimize unnecessary spending and inflationary pressures. As I will develop, the structure of a credit program— that is, the eligibility requirements, terms and conditions, manner in which the credit assistance would be provided, inadequate provision for congressional control over the program, et cetera— can contribute to unnecessary spending and costs to the Federal Government.

### **Duplication of programs**

Enactment of a credit program, absent a demonstration of clear need, would result in confusion on the part of potential applicants as to Federal agency responsibility, duplication of Federal agency activities, and inefficient use of Federal resources. In this regard, I understand that loans for alcohol plants and alcohol fuel plants are available under programs now conducted by the Farmers Home Administration in the Department of Agriculture, the Economic Development Administration in the Department of Commerce, and the Small Business Administration. In addition, there are pending proposals, such as Chairman Moorhead's bill, H.R. 3930, which would provide a variety of financial incentives for synthetic fuels production, including alcohol fuels.

### **Credit needs test**

Most credit programs are intended to facilitate the flow of credit to borrowers who are unable to obtain credit in the private market. The needs of more creditworthy borrowers are expected to be met in the private market without Federal credit aid. Accordingly, we believe it is essential that an applicant for a direct loan demonstrate that credit is not otherwise available on reasonable terms. Such a requirement would help direct Federal credit assistance to cases of demonstrated need, minimize unnecessary demands for Federal credit assistance, reduce Federal competition with and duplication of the activities of private lenders which would otherwise make the loans, and provide a built-in control over program growth. There is no such requirement in section 2 of H.R. 3905.

### **Interest rate subsidies**

In H.R. 3905, the interest rate on direct loans would be determined by the Secretary of Agriculture, except that the rate could not exceed the current average yield on outstanding marketable obligations of the United States of comparable maturities plus 1 percent. We believe that provision for a statutory ceiling on the interest rate which may be charged on direct loans should also be accompanied by a floor on such rates. Otherwise, a submarket rate of interest would stimulate increased demands for loans, and this problem would be exacerbated by not requiring the borrower to demonstrate that credit is not otherwise available on reasonable terms. Without such an interest rate floor, there will be inevitable demands to charge lower interest rates for particular projects or preferred borrowers. Unless the interest rate actually charged is sufficient to cover the Treasury's borrowing costs, as measured by current market yields on outstanding obligations of comparable maturities, and program administrative expenses and probable losses, the result will be hidden subsidies to program borrowers and costs to the Federal Government. In this regard, it is not clear that the additional charge of up to 1 percent would be sufficient to cover program administrative expenses and losses.

With respect to the interest rate formula in section 2, we believe that a determination of the current average market yield on outstanding obligations of the United States should be made by the Secretary of the Treasury and certified to the Secretary of Agriculture. The actual interest rates charged would then be determined by the Secretary of Agriculture under the authority which permits the Secretary of Agriculture to charge more than the current average market yield.

### **Federal guarantees of tax-exempt obligations**

The interest on obligations of public bodies is generally exempt from Federal income taxation. The authority in section 2 to guarantee loans to public bodies would result in Federal guarantees of tax-exempt obligations. The Treasury opposes Federal guarantees of tax-exempt municipal bonds. They create a class of securities which is stronger than the Federal Government's own securities. Like Treasury securities, they would be backed by the full Federal credit but, unlike Treasury securities, they would be exempt from Federal taxes. In addition, such guarantees would convey the benefits of both the Federal credit and the tax exemption to high-income taxpayers—the principal buyers of tax-exempt securities. Also, tax-exempt guarantees are an ineffective means of delivering Federal aid to local governments, since much of the benefit goes to high-income investors and since the financing of Federal programs in the municipal market competes directly with other State and local bond issues for essential local public facilities and increases the cost of financing the facilities. For these reasons, we believe that municipal bonds should only be guaranteed if they are taxable securities. On at least 19 occasions in recent years, Congress has enacted legislation which specifically prohibits Federal guarantees of tax-exempt obligations and provides other, more efficient means of financing credit assistance to public bodies, including assistance to public bodies under other provisions of the Consolidated Farm and Rural Development Act of 1972.

### **Coordination with Treasury financing**

There is no provision for Treasury coordination of the financing of obligations guaranteed under the bill. Requiring the approval of the Secretary of the Treasury of the interest rate, timing, and other terms and conditions of guaranteed obligations helps assure more efficient financing of these obligations and coordination with the financing of other Government and Government-backed obligations in the securities market. Also, in this regard, limiting the guarantee to private lenders, as proposed in section 2, could result in excessive financing costs because the Federal Financing Bank would be precluded from purchasing the guaranteed obligations. The Federal Financing Bank was created in 1973 for the stated purpose of reducing the cost of Federal and federally assisted borrowings from the public.

### **Other loan terms and conditions**

There is no authority in the bill for the Secretary of Agriculture to charge a guarantee fee. Failure to charge a guarantee fee in an amount sufficient to cover administrative expenses and probable losses will result in hidden subsidies to guaranteed borrowers and costs to the Government. Requiring an affirmative finding of reasonable assurance of repayment prior to making or guaranteeing a loan, limiting the maximum maturity of the loan to less than the useful life of the project, and requiring the borrower to have an equity stake in the project will help minimize Federal exposure to loss under the program.

### **Congressional control**

In the 1980 budget the administration proposed the establishment of a system of control over Federal credit programs based on annual limitations on gross loan activity for both direct lending and loan guarantee programs. Under the administration's proposal, annual limitations on gross lending for direct and guaranteed loans would be established in the regular budget and appropriations process. Yet, there is no provision in the bill that would limit annual direct and guaranteed lending under the program to amounts specified in annual appropriations acts. Such a provision would provide a firm basis for congressional control over annual activity under the program. Firm congressional control, in turn, would help to minimize unnecessary pressures on our credit markets.

In conclusion, the Treasury Department believes that the deficiencies in program structure will generate unnecessary demands for Federal credit assistance, resulting in unnecessary spending, and thus tend to contribute to inflationary pressures. Accord-

ingly, the Department recommends against enactment of section 2 of H.R. 3905 in its present form.

**Exhibit 19.—Statement of Secretary Miller, November 14, 1979, before the Senate Committee on Banking, Housing and Urban Affairs, on Federal loan guarantees for the benefit of Chrysler Corp.**

The administration seeks your support for authority to provide up to \$1.5 billion in Federal loan guarantees for the benefit of Chrysler Corp. on the condition that the company raise on its own \$1.5 billion of new cash or savings from third parties on an unguaranteed basis. We believe that this \$3 billion will finance the company through 1983 and enable it to reemerge as a commercially viable, self-financing entity.

My testimony will cover four major areas: First, the arguments for Federal financing assistance in this case; second, the company's current business and financial situation; third, its financing needs; and fourth, our specific legislative proposal. Attached are appendices that provide additional detailed information on certain issues.<sup>1</sup>

**Reasons for Federal financing assistance in this case**

This administration approaches Federal financing assistance to private corporations with great caution. Normally, corporations should be financed in the private markets, but there are cases in which exceptions should be made. We think that Chrysler represents one such case.

Chrysler is the 10th largest industrial corporation in the United States. Its 1978 revenues were \$13.6 billion, generated almost entirely from the sale of 1.2 million cars and 490,000 trucks. Its employment at the beginning of this year was 131,000 and today approximates 113,000. Approximately a quarter of a million others are employed by Chrysler dealers and principal suppliers. In addition, the company is the largest employer in Detroit and operates 25 of its total of 44 production facilities in the State of Michigan.

The alternative to a Federal aid program appears to be reorganization under the bankruptcy laws. Such reorganization would be costly. On the other hand, loan guarantees authorized now might prove to be costless if they are based on operating and financing plans which cause Chrysler to emerge from its present problems as a viable concern which no longer needs governmental assistance.

Our view of the costs of bankruptcy may be less bleak than some of the "worst case" predictions which have been publicized recently. But those costs would probably be greater than the cost of this proposed legislation. In any event, those costs, as summarized below, should be avoided if possible. They are described at length in appendix 1.

- A Chrysler bankruptcy could cost the Federal Government more than \$1.5 billion in 1980 and 1981 alone. We estimate the Federal cost for those years at a total of at least \$2.75 billion, an amount that includes loss of revenues, unemployment claims, welfare costs, and other incidental costs. Furthermore, there would be a substantial cost to the State and local governments. Moreover, this does not take account of any cost to the Pension Benefit Guarantee Corporation on Chrysler's unfunded vested pension fund liabilities of approximately \$1.1 billion, which would ultimately be borne by other pension fund sponsors.

In addition to these out-of-pocket costs, other serious adverse effects of bankruptcy would include:

- A serious direct impact on the people that work for Chrysler, its dealers, its suppliers, and for their families. There are now approximately 113,000 Chrysler employees, about an equal number of employees of its dealers, and

<sup>1</sup> Not included in this exhibit.



150,000 employees of its suppliers. Many would be affected. Conservatively, unemployment would increase by 75,000 to 100,000 during the 1980-81 period.

- A serious impact on Detroit, the State of Michigan, and other areas in the Midwest region, as well as specific localities around the country—not only where Chrysler has plants, but in places where automotive suppliers and dealers operate. Substantial unemployment and economic distress would occur in certain areas. More than half of Chrysler's workers (over 60,000 employees) are located in Detroit; and there are an additional 20,000 Chrysler employees in the rest of Michigan, with more than 40,000 supplier employees located in Michigan. Unemployment in the Detroit area could increase up to approximately 4 percentage points from its already high level of approximately 8 percent.
- The need to maintain a competitive domestic auto industry. Without Chrysler, the two remaining major domestic producers would represent a very narrow competitive base. This would be especially troublesome given current concerns about the strength of the competitive process and the high barriers to entry. Chrysler has exercised an important competitive role in challenging GM, Ford, and others throughout the market, despite its current lack of profitability. Its recent success in the subcompact market is indicative of its competitive importance.
- The potential loss of Chrysler's current and planned increases in capacity in the small-car market, at a time when the amount of small-car, domestic capacity is critical for trade, environmental, and other reasons.
- Important, negative effects on the U.S. balance of payments because Chrysler's production would be displaced by substantial foreign imports. The negative impact could be up to \$1 billion per year through 1981 from increased imports, largely of subcompacts but also of other models. Automobiles are a crucial industry, competing on a worldwide basis.

Our conclusion is that Chrysler can recover as a result of this proposed financing plan. It makes more sense than a reorganization in bankruptcy. It is not clear that the company's consumer franchise could survive a reorganization in bankruptcy and that a viable automobile company could emerge.

### **Chrysler's business and financial condition**

Chrysler's current predicament reflects the long-term transformation of the U.S. auto industry, Chrysler's difficulties in coping with it, and the particular 1979 weakness in the auto and the truck industries.

The combination of radical changes in industry product and mix dictated by foreign competition, energy cost changes, and Federal environment and safety regulations has indicated a basic redesign of the automobile. By far the most significant aspect of this has been the market shift toward small fuel-efficient cars. Such cars represented 16 percent of the total market in 1968; now they represent 35 percent, and are projected to increase to 60-80 percent by 1985.

It is estimated that the industry as a whole will spend approximately \$80 billion over the 1979 to 1985 period to implement this product line transformation. These amounts are so large as to stretch the financing capacity even of General Motors and Ford, both triple-A-rated borrowers, let alone Chrysler. Indeed, while Chrysler's 1980-85 capital spending is planned at \$13.6 billion, one of the larger 5-year capital budgets in the U.S., this is only 40 percent of GM's planned spending over the same period.

It is exceedingly difficult for Chrysler to finance this transformation. The company has long been the weakest of the three major domestic manufacturers, with a high cost structure, small market share, greater balance sheet leverage, and other fundamental weaknesses. Its net profit margin for the period 1969-78 has averaged only 0.7 percent. Chrysler incurred heavy losses during the last half of this period, while GM and Ford averaged 5.1-percent and 3.2-percent net margins. For the 10-year period ending in 1978, Chrysler's aggregate earnings were \$720 million, a very marginal return on its large revenue and asset base. It experienced losses of more than \$200 million in both 1975 and 1978. Appendix 2 provides additional historical information.

Until recently, Chrysler had intended to address this problem on its own. Beginning in 1977, the company initiated a major capital expenditure program to upgrade plant and equipment and develop new products to permit it to compete in the market of the 1980's. In addition to compensating for past deferrals and making other improvements, this program was aimed at improving its product line and meeting Federal regulatory requirements. To finance this program, Chrysler began a retrenchment in which it disposed of most of its foreign operations and took other actions to increase the availability of funds.

Chrysler's ability to generate funds through earnings was eroded, however, by the gasoline crisis of this past spring and the economic slowdown. Domestic automobile industry sales have been slow in 1979, falling 9 percent from 1978 levels through September, and 17 percent below last October's rate. Chrysler's sales have been even weaker, however, falling by 14 percent and 24 percent for the two respective periods.

Some of the earlier losses in volume were recouped through an aggressive rebate program. However, the rebates resulted in substantial losses on sales. The company lost \$721.5 million through September and projects losses of \$1,073 million for the year and \$482 million for 1980.

Chrysler's worsening financial situation has prompted some creditors—both lenders and suppliers—to withdraw or to seek to reduce credit in an attempt to protect their positions against a failure.

### Chrysler's financing needs

Let me turn now to a review of Chrysler's aid request and our analysis of it and of the company's future.

*The company's request.*—On October 17, Chrysler submitted a request for up to \$750 million in Federal loan guarantees. This amount reflected the company's attempt, at Treasury's request, to minimize its need for Federal financing help and to address various other questions posed by Treasury.

The Chrysler aid request was based on a 6-year business and financial plan. The company's strategy is to remain a full-line automobile and truck producer. It projects capital spending of \$13.6 billion over this period to modernize that product line and to comply with regulatory requirements. Furthermore, operating losses are projected through 1980 before a return to profitability in 1981.

The plan also forecasts an unfunded, cumulative cash flow deficit of \$2.1 billion through 1983. This assumed the continuation of those financing commitments which existed on October 17. Any reduction in these commitments would increase the company's need for Federal financing assistance.

The October 17 plan assumes that Chrysler would meet \$1.350 billion of the \$2.1 billion shortfall from non-Federal sources: \$850 million from "asset dispositions, financial institutions, State and local governments and others"; and \$500 million from "constituents and employee participation."

The bulk of the Federal financing assistance would be required during 1980 and 1981, when Chrysler projects financing shortfalls of \$1.5 billion and \$400 million, respectively, with an additional shortfall of \$201 million in 1982. A return to positive cash generation is projected beginning in 1983. The schedule for Federal assistance is unspecified, since it would depend on the timing of assistance from other sources.

Booz, Allen & Hamilton, the company's consultants on product planning, have recently expressed their view that the company's funding needs may exceed the levels of the October plan. On October 22, these consultants issued a report which recommends provision for contingencies of up to \$700 million to meet variations that are "more probable than not" in industry sales, shifts in market shares, and ability to achieve profit improvements. This \$700 million addition to Chrysler's original estimates of financing needs means a total 3-year need, in Booz Allen's view, of at least \$2.8 billion.

Booz Allen also recommends additional operating cost reductions, and a detailed study of alternative capital expenditure and product strategies to help reduce Chrysler's capital needs. In this regard, it indicated that the company itself is considering alternate product plans to reduce its needs should other risks materialize.

*The administration's view on the company's financing need.*—Based on the October plan, Treasury has concluded that the appropriate level of Federal loan guarantees is \$1.5 billion, rather than the \$750 million which was originally requested. This reflects our judgment that the company's gross financing need over the 1980–83 period approximates \$3 billion and that up to, but no more than, half of this amount should take the form of Federal loan guarantees.

Several factors have led to this recommendation for significantly larger financing assistance. One major reason has been the recently worsened outlook for the auto industry in 1980 and 1981. There have been major industry changes. For example, Data Resources, Inc., has dropped its forecast of auto industry sales to 9.8 and 10 million units for 1980 and 1981, respectively, from its earlier projection of 10.6 and 10.3 million. Furthermore, other forecasters have similarly reduced their estimates and Chrysler itself has also done so. A second factor is the results of Treasury's own analysis of the company's financing needs, which was completed last week with the help of outside experts. Let me turn now to a review of that analysis.

*Nature of Treasury review.*—In our review of Chrysler's financing request, we have been assisted by the accounting firm of Ernst & Whinney, which assigned more than 25 professionals to this matter, and by John C. Secrest, a former group vice president of American Motors Corp.

Throughout our efforts, we also had regular consultations with other Federal agencies on matters within their expertise, and special assistance from the staff of the Federal Reserve System. In addition to Chrysler submissions which are now public information, we have analyzed, reviewed, and challenged private Chrysler information and internal plans and had numerous meetings with Chrysler officials and staff.

Together with our consultants, we reviewed historical data on Chrysler for insights into its operations and any implications that might bear on future projections. We also studied the company's accounting practices and control and management systems. We then addressed the plan's revenue projections, the underlying profit improvement program, and related capital expenditure program, since these are the key elements.

A data base and computer model were prepared to test the company's projections at varying levels of industry sales, market share, and profit margins. We tested Chrysler's projections at 95 percent and 90 percent sales achievement levels in order to clarify the potential range of results. And finally, the plan was adjusted for possible shortfalls in profit improvement programs and other programs, and that series was also tested versus the 95-percent and 90-percent achievement levels. A complete exposition of our analysis of the October 17 Chrysler submission is attached as Appendix 3.

*Base case 1.*—Specifically, the Chrysler submission adjusted for the following major changes became base case 1:

- Projected industry sales for 1980 and 1981 were reduced from 10.5 million and 11.1 million units to 9.3 and 10.3 million, respectively.
- The wage concessions of \$200 million for 1980 and 1981 incorporated in the recent UAW contract were included. The October plan had assumed a GM-type settlement.
- Cost savings from Chrysler's variable margin improvement (VMI) and fixed-cost reduction (FCR) programs were reduced from \$6.87 billion to \$6 billion over the 6-year period of the plan.
- Correction of computational and other errors.

*Base case 2.*—Second, a more drastic revision of the Chrysler plan base case 1, based on our best judgment of Chrysler's likely ability to achieve the plan's basic assumptions. These revisions required the following major changes:

- Reduction of projected savings in Chrysler's VMI program in light of its ability to achieve its goals by reference to its existing programs and its history of difficulty in obtaining cost improvements.
- Adjustment of the FCR program. Advertising and sales costs were modified to reflect the projected volume reductions. An assumed cost was added for additional rebates that we believe may be necessary in 1980 and 1981.



*Adjusted base case 2.*—A third case makes two other adjustments and addresses possible reductions in the company's spending, as described below. Our judgment is that this "adjusted base case 2" approach presents the most realistic operating plan.

This case adds back the \$200 million UAW wage contribution to be consistent with using the company's October 17 submission as the base. This addition is offset by deducting a \$250 million cushion in cumulative contingency reserves through 1983 that Chrysler included in its submission. Elimination of this cushion was justified by the much more conservative assumptions underlying our adjusted base case 2.

More than \$1 billion in 1981, 1982, and 1983 capital spending, largely for post-1983 purposes, could be eliminated without resulting in a fundamental reduction or "downsizing" of the company. This reduced capital spending would save approximately \$950 million in cash by 1983.

The following table compares cash shortfalls under the Chrysler October 17 plan and each of the adjusted plans I have described:

	Cumulative funds required [\$ million]			
	1980	1981	1982	1983
Chrysler plan of Oct. 17 .....	1,554	1,915	2,116	2,113
First base case:				
100% base volume.....	1,472	1,959	2,266	2,342
95% .....	1,571	2,230	2,773	3,133
90% .....	1,669	2,502	3,280	3,923
Second base case:				
100% base volume.....	1,593	2,308	2,860	3,261
95% .....	1,689	2,572	3,351	4,025
90% .....	1,784	2,836	3,843	4,789
Adjusted base case 2:				
100% base volume.....	1,593	1,994	2,196	2,309
95% .....	1,689	2,258	2,687	3,073
90% .....	1,784	2,522	3,179	3,837

From these analyses Treasury concluded that Chrysler needs \$3 billion. Based on the company's estimates, it seems reasonable to suppose that the company could raise at least half that amount.

We considered the potential for a major "downsizing" of the company, as American Motors has done. The nature of Chrysler's operational structure and dealer system does not appear to permit this over the short term, however, without a severely disruptive effect. On the other hand, there may be some potential for alternatives of this nature over the long term, and we intend to pursue these. Chrysler has agreed to report on such alternatives by mid-December. If further study reveals that a less expensive solution can be devised without impairing Chrysler's long-term viability, we would be favorably disposed toward it, since a less ambitious plan would entail a lower level of Government involvement.

Treasury's judgment is that a \$3 billion financing plan has the potential of assuring the company's viability. There can be no assurance of success with this or any other plan, but we believe that the financing approach is sound and that the underlying business plan can remedy Chrysler's weaknesses. Nonetheless, even with \$3 billion, Chrysler's situation will remain very tight and the company must consider achieving additional efficiencies to provide adequate additional cushions against potential long-term risks.

*Regulatory burden.* —In formulating this \$3 billion plan, the administration has not attempted to justify Federal assistance on the basis that Chrysler is burdened by excessive costs of complying with Federal environmental and safety regulations.

- It would raise difficult policy problems, both with respect to the purposes of the regulations and equity vis-a-vis other producers. The administration has already sought to eliminate unnecessary burdens of regulation.
- Regulation is only one of the many elements and costs in the environment in which Chrysler operates. All companies must bear the cost of regulation in their industries.

- There has been no persuasive evidence that Chrysler would not be in the same dilemma now without these regulatory requirements. Chrysler has been unable to quantify adequately the portion of its financing needs which relate to compliance with regulatory requirements.

### The administration's legislative proposal

Our analysis shows that Chrysler requires \$3 billion of financing to make the transition to the auto market of the 1980's. The primary building block for this financing must be \$1.5 billion in commitments from non-Federal sources. The United States would provide the balance needed, up to \$1.5 billion. In this way, the Federal Government would serve as a partner to these private groups, not the company's dominant financier.

By requiring appropriate levels of contributions from all those who have a financial stake in the health of Chrysler, we test whether these contributions can really turn Chrysler into a viable concern, capable of repaying its new debt. Presumably, private investors will not provide additional financing to the company unless they are convinced that Chrysler can repay the new amounts borrowed.

The Federal loan guarantees would be made available, therefore, only if Chrysler obtains at least \$1.5 billion of new funds from non-Federal sources. If the non-Federal portion is not obtained, Federal loan guarantees would not be provided, since the resulting shortfall would frustrate this rescue effort.

Only new resources beyond those considered by Chrysler in determining the \$2.1 billion shortfall on the October 17 plan would count against this non-Federal assistance. Effectively, this would freeze into place at least those short-term credits outstanding on October 17. For example, to the extent that any bank or other credit resource of the parent is reduced subsequent to October 17, it must be replaced to maintain the base of credit which then existed.

To qualify, the non-Federal assistance is to be from the following types of sources: (i) financing commitments or concessions from parties with an existing financial stake in Chrysler's health; (ii) capital obtained through merger or sale of equity securities, or otherwise; and (iii) the proceeds of asset dispositions.

The specific level of assistance from any category or participant would be left to the company and its interest groups to work out; however, to the extent practicable, we expect Chrysler to obtain assistance from all sources, consistent with their stakes in Chrysler, and, as a practical matter, its needs should require all to participate. Probably the most immediate and most significant assistance would be from all those that would be directly affected by failure:

- Banks, financial institutions, and other creditors who would benefit by avoiding a default or bankruptcy and who would continue to profit from their relationship with Chrysler. In addition to firming existing commitments for the period of Federal aid, they could help satisfy this need by providing additional financing and restructuring existing debt to reduce debt service or subordinate their loans so as to facilitate additional more senior borrowings.
- Suppliers who would benefit in a similar way, and who might liberalize their credit terms and provide price concessions.
- Labor unions and employees who would benefit from continued employment could provide additional compensation and work-rule concessions or provide direct financing.
- State, local, and other governments who would benefit by the revenue from Chrysler's continued economic activity and would want to avoid the costs of its failure might provide direct loans, grants, or tax concessions.
- Dealers who would avoid current losses and retain the potential for future earnings might reinvest part of their profit in Chrysler.
- Shareholders and other investors who would avoid the potential for immediate loss and retain the potential for future earnings might make additional investment in the company or have their investment diluted.

- Asset dispositions will also provide a major source of cash to the company. The company owns several large assets which are marketable and where continued ownership by Chrysler is not crucial to the company's business success.

In addition, an equity capital infusion is important to strengthen the company, since the company requires a much larger equity base than it now has. Chrysler has been unsuccessful in its efforts in this area in part because of its current precarious position. With Government aid, it should be a more attractive candidate for equity financing. We intend to make certain that Chrysler pursues this avenue vigorously.

*Safeguards.*—The bill includes specific provisions to maximize achievement of the aims of assistance and to protect the Government's position:

- *Sound operating and financial plans.* Before a guarantee commitment could be issued, Chrysler would be required to submit a satisfactory 4-year operating plan for the period through 1983 which demonstrates that the company will emerge viable and self-financing thereafter. It would also be required to provide a financing plan through 1983 which demonstrates that it can satisfy its projected financing needs under the operating plan, including assurance of at least the minimum of \$1.5 billion from other sources. Both the operating plan and the financing plan must be accompanied by satisfactory assurances of feasibility and be updated at least annually so long as any guarantees are outstanding. Before actually guaranteeing any loan, the Secretary must find that those conditions of the plans continue to be satisfied.
- *Continuation of present financing commitments.* Maturities on the present financing commitments, and the \$1.5 billion of new commitments which will be obtained, must be no shorter than the maturities on Federal guarantees involved. The guarantees may not be issued at a faster rate than the other commitments are utilized.
- *Reasonable prospect of repayment.* Throughout, the bill includes provisions to further minimize the financial risk to the United States. Before committing and issuing guarantees, the Secretary must determine that there is reasonable prospect for the repayment of a guaranteed loan. In addition, the guaranteed loans must mature by 1990, in order to preclude Chrysler's long-term dependency on Federal aid.
- *Restrictive covenants.* Guarantee and loan agreements are to include all affirmative and negative covenants and other protective provisions that are usual and appropriate to transactions of this nature; these terms will not be amended or waived without the Secretary's consent.
- *Security required.* Unless the Secretary otherwise determines necessary and finds there to be adequate assurance of repayment, security must be obtained, existing loans must be subordinated, and dividends prohibited. The Secretary can waive the technical bankruptcy priority of the United States only if he also finds there to be adequate assurance of repayment without the priority; and he may not waive it so as to subordinate the position of the United States.
- *Payments to the Government.* The Government would receive an adequate return for its participation. At a minimum, it must receive a guarantee fee of at least one-half percent per annum. The Secretary could also negotiate additional compensation. Chrysler would be required to pay an appropriate interest rate on the loan. If the program is successful, it will produce no direct cost to the Government.

The negotiation of the non-Federal financing for Chrysler will be a long and complex process. Our experience in the New York City guarantee program demonstrates the need for flexibility to accommodate the variety of problems which inevitably arise in this process. Thus, while the legislation builds in a number of these protections for the Federal investment, it also permits sufficient flexibility to permit the financing package to be assembled.

*Employee stock ownership.*—There has been considerable discussion of linking Federal assistance to the establishment of an employee stock ownership program (ESOP). Employee ownership of industrial enterprises provides employees a direct stake in the profitability of the employer.



Certain of the ESOP proposals made to date, however, have been troublesome because they would use part of the Federal guarantees to support loans to an ESOP trust for the purchase of Chrysler stock. The loans would be repaid solely from Chrysler contributions to the trust. The employees get the stock, but pay nothing for it. In the Chrysler situation, it is important that significant contributions be made by each group with a substantial economic stake in recovery of the corporation. Thus, any grant of stock to Chrysler employees must be tied to commensurate cash or cash-like contributions from them.

The administration could support an ESOP for Chrysler which involves: (1) Payment by employees for a substantial portion of the value of Chrysler common stock purchased (this payment could be made over a short period of time through a payroll deduction program); and (2) availability of participation on a fair and nondiscriminatory basis. Payment of a reasonable purchase price provides Chrysler needed equity capital. Also, the bargain purchase nature of the plan would mandate a sacrifice from existing shareholders by diluting their present stake in the company.

### Conclusion

In closing, let me emphasize that no guarantees will be issued until the full amount of non-Federal assistance is committed. This means that, as in the case with the New York City assistance program, the ultimate resolution of the Chrysler problem may extend beyond enactment of this legislation. It may be resolved only after extensive negotiations that end in legally binding loan agreements and financial commitments.

In the last analysis, there are three key points underlying our recommendations to Congress on Chrysler. First, the administration believes that Federal financing assistance is justified in this case. Second, estimates of the company's financing needs have been carefully prepared and appear reasonable. Finally, we have submitted responsible legislation which would adequately protect the Federal interest. We urge your support for it.

### Exhibit 20.—Statement of Assistant Secretary Altman, January 28, 1980, before the Senate Committee on Banking, Housing and Urban Affairs, on Treasury activities under the New York City Loan Guarantee Act of 1978

I appear before you today to discuss the Treasury Department's activities under the New York City Loan Guarantee Act of 1978. My testimony will cover the following major areas:

- A recent history of the city's budget and financing developments including the Federal guarantees of city debt and the conditions under which these guarantees were issued;
- The status of the city's fiscal year (FY) 1980 budget, and the program to eliminate the gap (PEG) for FY 1981 and FY 1982; and
- A discussion of several key problems affecting New York's financial future, including prospects for the city's regaining access to the public bond market.

### Recent developments

Let me put this issue into some perspective by briefly reviewing the history of the New York City fiscal crisis.

It erupted in 1975 when the city lost access to conventional lending sources and teetered on the edge of bankruptcy. The city lost its ability to borrow because it was incurring enormous budget deficits and had already borrowed huge amounts to finance them. Lenders had lost confidence in the city's ability to repay.

The State of New York then undertook massive efforts to solve the city's fiscal problems. Among other things, it established the Municipal Assistance Corporation (MAC), the Emergency Financial Control Board (EFCB), and advanced \$800 million to the city. It was not until Congress passed the New York City Seasonal Financing Act of 1975, however, that the city was actually saved from apparent bankruptcy.

In the intervening 4 years, New York has met each of its budget goals since Federal credit assistance was first provided in late 1975. It intends to achieve real budget balance—balance in accordance with generally accepted accounting principles (GAAP)—in its fiscal 1981, a full year ahead schedule.

Several important recent financial strides deserve mention:

- The city's 1980 budget will reduce its GAAP deficit to approximately one-fifth of the 1976 level and the city's budget has been balanced for the last 2 fiscal years in accordance with State law.
- The city's proposed 1981 budget entirely eliminates its GAAP deficit. This compares to a \$1.8 billion GAAP deficit in FY 1976.
- The city was independently audited for the first time in fiscal year 1978 and this was repeated last year.
- The overhang of short-term debt has been funded. Indeed, its short-term borrowing needs have been cut from as high as \$8.4 billion in 1975 to \$600 million in fiscal year 1980.
- The city reentered the public credit markets in 1979 for the first time since 1975. Two city sales of short-term notes totaling \$275 million were oversubscribed by investors and only \$375 million of the \$750 million pension fund/bank standby credit line was used in fiscal 1979. In fiscal 1980, the city has already sold \$375 million of its notes to the public and now expects to sell up to \$225 million more in the public markets, thereby avoiding any use of its standby credit facility, which now consists solely of financial institutions.

*Federal guarantees issued to date.*—Mr. Chairman, since I last testified before you in February 1979, Treasury has issued further Federal guarantees of city bonds as follows:

<i>Date</i>	<i>Amount</i>
February 15, 1979 .....	\$150 million
June 28, 1979.....	50 million
August 30, 1979.....	100 million
January 3, 1980 .....	<u>150 million</u>
Total.....	\$450 million

To date, the aggregate amount of city bonds guaranteed is \$650 million. An additional \$100 million of guarantees are scheduled to be issued next month. This would complete the \$750 million in Federal guarantees which are included in the \$4.5 billion long-term financing plan as "up-front" guarantees. The \$900 million of remaining guarantee authority will only be used in the unlikely event that both the City and MAC are unable to finance the city's long-term needs in the next 2 years.

The United States has received prompt quarterly payments from the city of the one-half percent guarantee fee provided under the Guarantee Act. At the end of December, these payments totaled \$2,070,053.47.

*The guarantees.*—On each issuance of Federal guarantees, Treasury must determine that the city is in compliance with the conditions of eligibility set forth in the Guarantee Act. Your Committee staff has been provided with copies of the formal determinations made before each issuance. I will devote a significant portion of my testimony reviewing the most important aspects of the city's compliance with the Guarantee Act—budget balance and credit market progress. I think it important, however, to mention briefly the city's compliance with certain other areas of the Guarantee Act.

*Reasonable prospect of repayment.*—Federal guarantees of city debt cannot be issued unless there is a "reasonable prospect" that the principal and interest on the outstanding guaranteed indebtedness will be repaid. Since these Federally guaranteed obligations have maturities of up to 14 years, Treasury evaluates this "reasonable prospect" in terms of the city's long-term fiscal and economic health. We have found that both the strength of the city's economy and the demonstrated local commitments to continued budgetary and financial reform enhance the security of the guaranteed debt.

One recent change in the financing program will be of interest to you, Mr. Chairman. According to the city's latest financial plan, in FY 1983 the city anticipates refunding \$180 million of its Federally guaranteed bonds. This represents 24 percent of the principal amount of guaranteed bonds projected to be outstanding by the end of FY 1980, exceeding the 15 percent refunding requirement under the Guarantee Act.

*Financing commitments.*—The local financial institutions and city pension funds have maintained their commitments to purchase unguaranteed Municipal Assistance Corporation securities. Also, MAC has sold its bonds to the public on schedule. We expect these parties to continue to meet their financing commitments in FY 1981 and FY 1982 in accordance with the city's financing plan.

*Independent fiscal monitor.*—Section 103(6) of the Guarantee Act requires that "an independent fiscal monitor"—the Financial Control Board—"has the authority to control the financial affairs of the City...." The Control Board has exhibited broad financial control, review and supervisory powers over the city on its course toward fiscal recovery.

*Financial reporting and accountability.*—Another aspect of the city's creditworthiness relates to the city's financial reporting and control systems. Since 1975 the city improved significantly in this area through the implementation of its Integrated Financial Management System (IFMS).

To comply with Section 103(7)(a) of the Guarantee Act, the city has been audited in 2 consecutive years by a consortium of independent certified public accountants. There are few large municipalities that can claim a like accomplishment.

Beyond this major improvement, and as a result of the Guarantee Act, the city has established an actively functioning Audit Committee in order to address and review major accounting issues affecting New York City. The improvement of the City's recordkeeping system, the implementation of annual independent audits, and the establishment of an Audit Committee are all positive developments.

### **The New York City budget**

The key to restoring New York's ability to finance itself is for it to attain true balance in the city budget and to maintain that balance. On this basis, institutional lenders and the credit rating agencies will regain confidence in the city's debt. The Guarantee Act recognized this by requiring the Treasury Department to determine, prior to each issuance of a Federal guarantee, that the city's budget is in balance under New York State law and that the city is making substantial progress toward balance according to GAAP in FY 1982.

*FY 1979 results.*—The city incurred a \$422 million deficit on a GAAP basis in fiscal 1979. This represented an improvement of \$290 million over the 1978 deficit level. Indeed, this improvement occurred even though \$116 million of revenues, originally projected for 1979, will be realized in later years. The principal reason that New York remains in GAAP deficit at all is its continued practice of funding certain operating expenses from its capital budget. The Guarantee Act requires the city to phase out this practice by budgeting no more than \$450 million of these so-called capitalized expenses in fiscal 1979, \$300 million in fiscal 1980, \$150 million in fiscal 1981 and zero in fiscal 1982. In fiscal 1979, the City voluntarily began to accelerate this phaseout schedule.

In contrast to the \$422 million GAAP deficit, under accounting principles prescribed by New York State law the city realized a \$216 million surplus in 1979. Thus, fiscal 1979 was a year of financial progress for the city.

*FY 1980.*—Fiscal 1980 has also been another year of budget improvement. In January 1979, the city announced its preliminary 1980 budget, that included a set of actions to eliminate a potential deficit under State law of \$433 million. These measures included up to \$250 million of city actions and at least an additional \$183 million in State and/or Federal assistance.

The actual 1980 budget, adopted in June 1979, was balanced on a State law basis. A substantial increase in city's revenue, in addition to a proportional mix of city, State, and Federal actions eliminated the potential deficit. Due to various uncertainties, the Financial Control Board (FCB) requested that the city detail a contingency program



of more than \$100 million of city actions if FY 1980 balance could not be maintained as the year progressed.

As fiscal 1980 unfolded, serious budget problems developed in the Board of Education and the Health & Hospitals Corporation (HHC). In December, the city was required to establish an additional reserve of \$50 million to cover potential budget gaps in HHC and allocate an additional \$19 million of support for the Board of Education.

Yet, stronger than expected revenue growth and further expenditure reductions enabled the city to tackle these mid-year problems and still remain in balance under State law without implementing the contingency program required by the FCB. Indeed, even though \$135 million of forecasted FY 1980 revenues are now targeted for FY 1981, the city's net revenues are projected at \$38 million above the adopted budget.

This reserve strength enabled New York to avoid in 1980 the type of sharp spending cuts which would have resulted if the city had to implement its contingency program. It might have been wise to voluntarily reduce city expenditures further, in light of the large potential 1981 and 1982 budget gaps, but the city chose a milder course.

*The fiscal 1981 and fiscal 1982 budgets.*—On January 16, Mayor Koch released his preliminary 1981 budget. The Treasury Department has had only 11 days to evaluate this plan and our conclusions, therefore, are highly preliminary. We are not required by the Loan Guarantee Act to make findings concerning the success of this plan until the next issuance of guarantees, currently scheduled for February 21.

The PEG plan would attain the long-sought goal of true budget balance according to GAAP next year. This would be 1 year earlier than required by Federal and State law and is a courageous step.

The city estimates that attaining this FY 1981 goal will require eliminating a potential deficit of \$677 million. Moreover, if this 1981 gap is not closed, it will grow to approximately \$1.1 billion in 1982. Certain fiscal monitors, using various 'worst-case' assumptions, have estimated considerably larger potential gaps in each of these years—in excess of \$1 billion in FY 1981 and growing to \$2 billion in FY 1982.

These estimated gaps are large, but it is important to put them into perspective.

*Background.*—Table I below compares the city's performance against its budget goals for FY 1976–79. As you will note, the city has met or exceeded each of its budget goals over this period.

TABLE I.—*Actual budget results compared with original budget goals*  
[\$ millions]

Fiscal year	City's goal under State law	Yearend budget results under State law	Yearend budget results under GAAP
1976 .....	\$1,051 deficit	\$968 deficit	\$1,822 deficit
1977 .....	686 deficit	329 deficit	1,039 deficit
1978 .....	Balance	32 surplus	712 deficit
1979 .....	Balance	216 surplus	422 deficit

The large differences between the original projections and the actual results reflect the inherent conservatism in revenue and expenditure assumptions in the city's budget methodology. In effect, the process itself requires that potential budget gaps be overstated.

Specifically, the city did not include nonrecurring revenues in its forecasts, even though varying amounts of such revenue occur each year. Furthermore, the city did not reduce its expenditure forecasts to reflect likely spending shortfalls ('underspending') even when such shortfalls appeared certain.

Finally, the city has generally used conservative assumptions to forecast its economically sensitive revenues. Actual revenues have frequently exceeded plan, as they did in FY 1980.

In short, the real budget gaps have invariably been smaller than the originally estimated gaps. This could again be the case in the future.

*Fiscal 1981.*—Last June, the city forecast a 1981 deficit of \$464 million on the State law basis. The recently released preliminary 1981 budget, however, estimated this gap at \$677 million. The principal elements of the 1981 deficit outlook are as follows:

- The Mayor's decision to reach budget balance 1 year early increases the potential deficit by \$275 million. This includes the elimination of \$150 million of incremental capitalized expenditures and \$128 million of incremental pension costs;
- Aside from this mayoral decision, Federal and State laws in effect already required the city to adjust for increases of \$50 million in pension costs and \$132 million in phased-out capitalized expenditures;
- An assumed 4 percent wage increase in 1981 (the same as that in 1978) which the city estimates will cost approximately \$142 million in that year. This is the first estimate by the City of its future labor costs;
- An increase in Medicaid payments, of which the city's share is \$102 million;
- A \$65 million increase in energy costs and a legally mandated \$64 million increase in expenditures for special education;
- These increased costs are somewhat offset by two categories of increased revenue: realization in 1981 of \$155 million previously projected for this year; and a revised estimate that 1981 city tax receipts will be \$33 million higher than the 1980 level.

*City deficit-reduction actions.*—The city has proposed \$507 million in its own deficit-reduction actions to help close this \$677 million potential gap. These include:

- Improved collection techniques and other steps resulting in \$33 million of increased revenue;
- The Mayor's decision to increase taxes and certain other charges to produce increased revenues of \$175 million. This includes \$39 million in increased water and sewer charges, \$36 million in increased real estate taxes, and \$35 million in increased excise taxes on beer and liquor;
- Expenditure reductions of \$299 million consisting primarily of \$165 million of reductions in the city's personnel budget and \$83 million of nonpersonnel reductions.

Table II details the major items in this city program.

TABLE II.—1981 New York City program  
[\$ millions]

<i>Revenue actions</i>	
Improved rental income collection.....	\$6
Increased license and permit fees.....	5
Reduced provision for disallowances.....	10
Increase in interfund agreements.....	5
Other.....	7
	<u>33</u>
<i>Tax and charge increase to yield \$175 million/year</i>	
Water and sewer charge increase.....	39
Real estate tax increase.....	36
Excise tax on beer and liquor.....	35
Financial corporation tax revision.....	20
City gasoline tax extension.....	13
Parking garage tax increase.....	11
Hotel Tax Revision.....	11
Tax on taxi medallion transfer.....	8
Real estate tax — veterans exemption.....	7
Other.....	12
	<u>192</u>
Less possible slippage.....	-17
	<u>175</u>

*Agency expenditure reductions*

Police .....	29
Fire .....	11
Correction .....	14
Social services .....	25
HRA .....	18
Board of Education .....	111
CUNY .....	5
All other .....	35
	<u>248</u>

*Other reductions*

Transit, housing, and other subsidies .....	9
HHC subsidy .....	20
Energy conservation program .....	12
OTPS cost containment .....	10
	<u>51</u>
Total .....	<u>507</u>

It will not be easy to realize the full \$507 million of projected city actions. Most of the revenue actions and tax increases will require the cooperation of the City Council and/or the State Legislature. Although tax increases are never popular, some local support for these actions has been reported.

Concerning spending, Mayor Koch has proposed major cuts in the personnel budget totaling \$165 million. This means a net reduction in city-funded jobs of approximately 5,000. It includes a net cut of 3,100 in education personnel, and 722 in the uniformed police force. The overall job reductions appear possible, although they may be particularly difficult in the education area.

Regarding nonpersonnel cuts, the \$83 million projected 1981 reduction also appears attainable. In each of the past 3 years, the city's actual reductions in this area have exceeded those projected in each January's PEG plan.

There are several uncertainties among these city actions, however, including the following:

- The ability of the Board of Education to sustain reductions of the magnitude proposed by the City while maintaining services at an acceptable level. New control procedures to provide additional oversight over the fiscal affairs of the Board have been instituted. These controls should facilitate the implementation of these cuts;
- The City's plan to reduce its subsidy to the Health and Hospitals Corporation (HHC). Present projections of HHC revenues are uncertain today. Although the city is under no legal obligation to fund HHC deficits, it has done so in the past;
- City expenditures for energy, which have been rising rapidly.

The City's 1981 plan also calls for unspecified State and Federal actions totaling \$170 million. It is simply too early to judge whether this estimate is realistic. Governor Carey's State budget was released only 1 week ago, and President Carter's proposed 1981 Federal budget will be released today. I will discuss in greater detail the prospects for intergovernmental aid in a later portion of my testimony.

*Fiscal 1982.*—Fiscal 1982 will be a more difficult year for New York City. Assuming the city is able to close the \$677 million gap in FY 1981, through significant and recurring city expenditure reductions, revenue actions and tax increases, and moderate increases of Federal and State assistance, a potential \$462 million budget gap still remains. The principal cost elements in this additional gap are:

- An additional \$189 million provided to fund a 4-percent wage settlement;
- \$75 million to cover increasing energy costs;
- An additional allocation of \$62 million of city funds for Medicaid;
- An additional \$49 million allocated to the Board of Education for Special Education.



There is considerable uncertainty, however, as to whether this \$462 million 1982 deficit estimate is realistic. It remains to be seen whether the city can negotiate fiscally restrained labor contracts covering 1981 and 1982. In addition, its projections call for a large increase in State and Federal aid for 1982, which will be difficult. Finally, the 1982 deficit will automatically be larger if the city fails to eliminate the full \$677 million 1981 potential gap on a recurring basis. A judgment on whether a large 1982 gap can be closed depends on an assessment of (1) whether the city has the capacity to make further large cuts, and (2) what can be expected of Federal and State aid in the out-years.

The city's plan proposes an additional \$222 million in city actions and \$240 million in State and Federal actions to close this gap. Table III shows the major items in the 1982 program, their combined 1981 and 1982 values as well as their incremental value.

As you will note from table III, the program the city proposes for fiscal 1982 consists primarily of actions initiated during the previous fiscal year. These actions have an increased value because they are expected to be more fully phased in during the latter year. Therefore, the comments I made regarding the 1981 program are applicable here as well. It is a matter of some concern that the city has not identified alternative programs for 1982 given the likelihood that some of the PEG actions will fail to meet the city's expectations.

TABLE III.—FY 1981–82 New York City program  
[\$ millions]

	Total value	FY 1982 incremental value
<i>Revenue actions</i>		
Implement semiannual		
real estate tax payments .....	\$32	\$32
Increase CUNY tuition .....	5	5
Continuation of 1981 actions .....	56	23
Total revenue actions .....	93	60
1981 tax and fee increases .....	175	—
<i>Agency expenditure reductions PS/OTPS</i>		
Police .....	38	9
Fire .....	17	6
Sanitation .....	9	7
Corrections .....	18	4
Social services .....	33	8
HRA .....	20	2
Board of Education .....	182	71
CUNY .....	6	1
All other .....	59	26
Total agency reductions .....	382	134
<i>Other reductions</i>		
Transit, housing and other subsidies .....	12	3
HHC subsidy .....	20	—
Energy conservation program .....	26	14
OTPS cost containment .....	21	11
Total other reductions .....	79	28
Total New York City actions .....	729	222

Since 1975, the city has shown the capacity to meet its budget goals and, year after year, it has eliminated huge projected deficits. The continuing commitment of city and State elected officials to the city's financial well-being is solid. Mayor Koch's resolve to reach a GAAP-balanced budget in FY 1981, a year ahead of an already rigorous schedule, is the best evidence of this commitment.

*State aid.*—New York State faces serious budget pressures of its own in its fiscal year 1981. Therefore, its recently announced Executive Budget is extremely tight. The combination of certain formula-driven increases in expenditures, tax-reduction programs and the possible impact on the State of a recession threaten future increases in aid to the City. Despite these budget difficulties, the State's commitment to the

city's recovery remains undiminished. During the State's fiscal years 1976-80 Governor Carey successfully supported significant increases in State aid to New York City. In FY 1980 alone, State assistance to the city increased by more than \$200 million.

*Federal aid in 1981 and 1982.*—Our preliminary indications of the President's FY 1981 budget proposal are that Federal aid to the city will continue to increase into the 1980's as it has every year since 1976.

Modest increases in aid to the city may be forthcoming, but they are in the area of legislation. I am referring to programs such as targeted fiscal assistance, countercyclical revenue sharing, and Medicaid and welfare funding reform.

Specifically, the two antirecession fiscal assistance programs (actually two parts of one bill), if passed by Congress in one of their present forms, would increase unrestricted aid to the city by as much as \$45 million in city FY 1981 and perhaps a greater amount in FY 1982, depending on local economic conditions. In addition, the administration is working on a proposal to broaden eligibility criteria for Medicaid, and the increased Federal reimbursement rate for the Aid to Families with Dependent Children (AFDC) program could free up additional city funds annually. None of these proposals, of course, are assured of passage.

In addition to these actions which will require legislative approval, the administration continues to work on a series of administrative actions, primarily in the area of public housing, that would provide recurring fiscal relief.

The more limited ability of the State to provide additional significant amounts of budget aid means that the City may require major increases in Federal fiscal assistance to meet 1981 and 1982 budget goals. Obviously, the Administration has provided assistance to the City in the past. It continues to work for legislative programs to assist this country's urban areas with their unique problems. We are hopeful that Federal assistance together with State and city actions will eliminate future budget gaps.

There are other areas of concern in the city's road to financial self-sufficiency. A discussion of these follows.

### **The national and local economy**

A major factor in evaluating the city's prospects relates to the impact of the projected recession. A national recession was widely projected to begin during the last quarter of 1979 and continue into late 1980. The mixed signs over the past few months raised some doubt about the timing and duration of the recession. The major forecasting agencies are now projecting a moderate recession that will be more severe than the downturn projected in the late summer, but not as severe as the 1974-75 recession. In any event, it appears the local economy is better prepared for a recession than it was in 1973: The City's employment levels, after drastic decline since 1969, have stabilized; the decline in manufacturing employment and a move toward service-oriented industries makes local employment generally less affected by cyclical swings in the economy; the automobile and construction industries appear to be on the leading edge of the forecasted recession—the city does not have a heavy dependence on automobile production, and commercial construction is experiencing a boom, particularly in the borough of Manhattan; and retail sales on a city-wide basis have continued to out-perform the national averages. Hence, if the severity of the recession is no worse than currently projected, our judgment is that the city's projections should not be seriously askew.

### **Wage settlements**

The city's estimates of budget deficits have not previously included the cost of potential wage settlements in FY 1981 and FY 1982. The city has now included in its baseline estimates the funding of a 4-percent wage settlement in FY 1981 and FY 1982. The prospective costs of such a wage settlement are estimated by the city at \$142 million in FY 1981 and \$331 million in FY 1982. Last Thursday the city's unions announced their unwillingness to settle for 4-percent annual increases as they did in 1978. On the other hand, Mayor Koch has indicated to the city's municipal labor leaders not to expect to receive the same increases provided in existing pacts—which

are 4-percent. Ultimately, the wage settlement will be negotiated, hopefully on reasonable terms, between the city and its unions.

### Capital spending

Another important factor in the city's attempt to achieve economic stability and financial independence is its capital spending program. Though not specifically related to the city's near-term financial future, the city's ability to provide an attractive environment for its citizenry and for economic development purposes will be an essential element in the city's long-term fiscal health.

One critical factor in support of the Guarantee Act was the establishment of a credible financing package for the city so that improvement of its physical plant could get back on track.

Four years of neglect caused by the city's fiscal crisis have left the city's infrastructure in a somewhat deteriorated condition. Yet, the city has been slow in using capital funds provided for rebuilding. We appreciate the massive job of totally reactivating a capital program which has been dormant for 4 years. Nevertheless, the city must make a maximum commitment to improve its capital planning process.

Early projections for FY 1980 capital spending were \$582 million. Subsequently, this estimate was lowered to \$440 million. The city's new Four-Year Plan, however, indicates further "slippage" to \$394 million. We have carefully monitored the city's capital spending and consider this estimate reasonable. In connection with this latest reduction, however, the city did indicate that the \$2.3 billion capital-spending goal in the FY 1979-82 period was reachable.

Over the last few months the city has shown signs of progress in this area by coordinating the activities of all city agencies under one central office and improving accountability throughout the capital budget system.

### Restoring access to the public bond market

A major factor in the restoration of the city's long-term fiscal and economic independence will be its ability to find adequate sources of long-term credit in the public markets. Under the Guarantee Act, the city must attempt to sell its own bonds to meet a portion of its long-term financing needs in FY 1980.

Moody's Investors Services currently rates the city's bonds "B," which is below investment grade. Until an investment grade rating is achieved, the city will experience difficulties in attaining significant market access. In its review of the city's credit, Moody's commented that "fundamental credit elements are demonstrably weak and the city's long-term general obligation bonds continue to lack the characteristics of a desirable investment." The other major rating agency, Standard and Poor's, has maintained its rating suspension of city securities since April 1975.

The absence of a suitable credit rating on its bonds has the practical effect of excluding, among other investment groups, banks, insurance companies, trust departments and municipal bond funds from purchasing long-term city bonds.

While there may be a limited demand for New York City bonds among individual investors, without the participation of institutional investors New York will not achieve full financing independence. The city has prepared a strategy to fully enter the public credit market.

The cornerstone of this strategy is to achieve budget stability and other management objectives which appear to be crucial in obtaining an investment grade rating. The city's budget progress in fiscal 1980 and its bold step in accelerating the phase-in of a GAAP-balanced budget for fiscal year 1981 can only improve its chances for an investment grade rating. The conclusion of the upcoming collective bargaining negotiations with the city's work force will resolve another major uncertainty.

As for tapping the limited, individual investor market for city bonds, Mayor Koch has stated that "the existence of this uncertain market, while encouraging, cannot serve as the basis of any long-range solutions to the city's credit needs, since it simply cannot provide the substantial amounts of capital regularly required by the city." Current market conditions and the uncertainties surrounding the forthcoming labor negotiations seem to mitigate against such an attempt prior to FY 1981.



*FY 1981 and 1982.* — As you are aware, Mr. Chairman, the city's financing schedule calls for it to sell \$300 and \$645 million of unguaranteed bonds to the public in FY 1981 and FY 1982, respectively. The Guarantee Act requires such an effort. Without an investment grade rating, however, institutional investors will be unlikely participants in such an offering. It is equally unlikely that the requisite amounts of bond sales under the Guarantee Act in FY 1981 and FY 1982 can be met solely through sales to individual investors on reasonable terms. Any amounts the city cannot finance independently are to be covered, in the first instance, by MAC.

If the city is unable to access the bond market over the next 2 years, MAC has sufficient bonding authority to issue, on behalf of the city, its own bonds. In addition, we believe that MAC will have sufficient market access so as to preclude the issuance of standby Federal guarantees.

The next 12 months will be pivotal in the city's self-financing quest:

- The conclusion of the forthcoming wage negotiations with the city and its municipal unions will eradicate a major uncertainty in the city's financial plans;
- The city will have provided a budget balanced in accordance with GAAP;
- A successful sale of a limited amount of bonds in the public market, without an investment grade rating, will demonstrate investor confidence in the city's fiscal progress.

These factors should facilitate the city's ability to achieve an investment grade rating — a critical step in the city's ultimate goal of financing independence.

I will close by emphasizing that the city has shown the willingness and wherewithal to take whatever steps are necessary to meet its statutory budget and financing requirements. The city's and State's commitment to continuing this record is clear. We, therefore, remain satisfied that the city, the State and other interested parties are making the maximum effort as required by the Guarantee Act to solve the city's fiscal and financing difficulties.

**Exhibit 21.—Statement of Secretary Miller, April 16, 1980, before the Subcommittee on Taxation and Debt Management of the Senate Committee on Finance, on financing requirements, bond authority, and interest rate on savings bonds**

My purpose here today is to advise you of the Treasury's financing needs through fiscal year 1981 and to request an increase in the authority to issue long-term securities in the market and removal of the statutory interest rate ceiling on savings bonds.

**Financing requirements**

The present temporary debt limit of \$879 billion will expire on May 31, 1980, and the debt limit will then revert to the permanent ceiling of \$400 billion. Prompt enactment of legislation is necessary to permit the Treasury to borrow to refund maturing securities and to pay the Government's other legal obligations.

Our current estimates of the amounts of debt subject to limit at the end of each month through the fiscal years 1980 and 1981 are shown in the attached table. The table indicates that the debt subject to limit will increase to \$881 billion on September 30, 1980, and to \$897 billion on September 30, 1981, assuming a \$15 billion cash balance on these dates. These estimates are consistent with the administration's March revision in the budget estimates. The usual \$3 billion margin for contingencies would raise these amounts to \$884 billion in September 1980, and \$900 billion in September 1981. Thus, the present debt limit of \$879 billion should be increased by \$5 billion to meet our financing requirements through the remainder of fiscal 1980 and by an additional \$16 billion to meet the requirements through fiscal 1981. However, as indicated in the table, the debt subject to limit reaches a seasonal peak in May 1981 of \$914 billion and then declines to \$897 billion in September, assuming a constant \$15 billion cash balance. Thus, we are requesting that the debt limit for FY 1981 be increased to \$910 billion, which would get us by the temporary May 29 peak with an adequate cash balance of \$11 billion on that date.

For your convenience, the deficit and debt figures for each year over the past decade are shown in the final table attached to my statement.

Let me emphasize the importance of timely congressional action on the debt limit. In mid-May the Treasury expects to announce offerings of new note issues to refund obligations which mature on May 31 and perhaps to raise new cash. Since May 31 is a Saturday, the obligations maturing on May 31 cannot be paid off or refunded until Monday, June 2, at which time the present debt limit authority will have expired. Moreover, we will also need to announce and auction Treasury bill issues in the third or fourth week of May. These do not settle until the first week of June. Thus, without an increase in the debt limit by mid-May, we will be forced to postpone offerings because delivery of the securities in early June could not be assured. Failure to offer these securities as scheduled could be disruptive of the Government securities market and costly to the Treasury.

Investors as well as dealers in Government securities base their day-to-day investment and market strategies on the expectation that the Treasury will offer and issue the new securities on schedule. Delayed action by Congress on the debt limit, therefore, would add to market uncertainties, and any such additional risk to investors is generally reflected in lower bids in the Treasury's auctions and consequently in higher costs to the taxpayer.

This Committee has made every effort in the past to assure timely action by Congress to increase the debt limit. Yet, the record of recent years has not been good. On three of the last five debt limit bills action was not taken before the expiration date, and the Treasury was unable to borrow until the Congress acted 2 or 3 days later. Significant costs were incurred by the Treasury, and extraordinary measures were required to prevent the Government from going into default. The Treasury was required to suspend the sale of U. S. savings bonds, and people who depend upon social security checks and other Government payments suddenly realized that the Treasury simply could not pay the Government's bills unless it was authorized to borrow the funds needed to finance the spending programs previously enacted by Congress.

It is essential that we do everything possible to maintain the confidence of the American people in their Government. Confidence in the management of the Government's finances was seriously undermined each time the debt limit was allowed to lapse, and we must all work to avoid that outcome in this instance.

### **Bond authority**

I would like to turn now to our need for an increase in the Treasury's authority to issue long-term securities in the market without regard to the 4¼-percent ceiling.

Under this administration, the Treasury has emphasized debt extension as a primary objective of debt management, a policy which we believe to be fundamentally sound. This policy has caused a significant increase in the average maturity of the debt, reversing a prolonged slide which extended over more than 10 years. In mid-1965 the average maturity of the privately held marketable debt was 5 years 9 months. By January 1976 it had declined to 2 years 5 months because large amounts of new cash were raised in the bill market and in short-term coupon securities. Since that time, despite the continuing needs for cash of the Federal Government, Treasury has succeeded in lengthening the debt to 3 years 10 months, currently.

Debt extension has been accomplished primarily through continued offerings of long-term bonds in our midquarterly refundings as well as regular offerings of 15-year bonds in the first month of each quarter. By developing the long-term sector of the market we have broadened the market and increased demand for Treasury securities. These longer term security offerings have also contributed to a more balanced maturity structure of the debt, which will facilitate efficient debt management in the future. Moreover, these offerings have complemented anti-inflation efforts. By meeting some of the Government's new cash requirements in the bond market rather than the bill market, we have avoided adding to the liquidity of the economy at a time when excessive liquidity is being transmitted into increasing prices.

Congress has increased the Treasury's authority to issue long-term securities without regard to the 4¼-percent ceiling a number of times in recent years, and in the

Debt Limit Act of September 29, 1979, it was increased from \$40 billion to the current level of \$50 billion. To meet our requirements for the remainder of the fiscal year 1980, the limit should be increased to \$54 billion; and to meet our requirements in the fiscal year 1981, the limit should be increased to \$70 billion.

The Treasury to date has used over \$45 billion of the \$50 billion authority, which leaves the amount of unused authority at less than \$5 billion. While the timing and amounts of future bond issues will depend on prevailing market conditions, a \$20 billion increase in the bond authority would permit the Treasury to continue its recent pattern of bond issues throughout fiscal year 1981. We are currently issuing long-term securities at an annualized rate of approximately \$14 billion.

### Savings bonds

In recent years, Treasury has recommended frequently that Congress repeal the ceiling on the rate of interest that the Treasury may pay on U.S. savings bonds. In the Debt Limit Act of April 2, 1979, Congress increased the statutory ceiling from 6 percent to 7 percent. The Treasury increased the savings bond rate to 6 ½ percent effective June 1, 1979. Then, in December 1979, the Treasury announced that the interest rate on a new 11-year series EE bonds, which went on sale on January 1, 1980, would be 7 percent for bonds held to maturity and that the rate on outstanding E bonds would also be increased to 7 percent for bonds held an additional 11 years. Legislation is necessary to provide for further increases beyond the present 7-percent statutory ceiling.

Mr. Chairman, we are concerned that the present requirement for legislation to cover each increase in the savings bond rate does not provide sufficient flexibility to adjust the rate in response to changing market conditions. The delays encountered in the legislative process could result in serious inequities to savings bond purchasers and holders as interest rates rise on competing forms of savings.

The Treasury relies on the savings bond program as an important and relatively stable source of long-term funds. On that basis, we are concerned that participants in the payroll savings plans and other savings bond purchasers might drop out of the program if the interest rate were not maintained at a level reasonably competitive with comparable forms of savings.

While the savings bond rate has increased relative to the 5 ½-percent regulatory ceiling on passbook savings in federally insured thrift institutions, the much greater increase in market interest rates over the past year has had a substantial adverse impact on the savings bond program.

Sales of savings bonds in 1978 reached \$8 billion, a peacetime record; but in 1979, as market interest rates increased, savings bonds sales fell to \$7 billion. In the first three months of 1980 sales were only \$1.4 billion, 26 percent below the first quarter in 1979 and 34 percent lower than sales in the first quarter of 1978.

The major problem, however, has been on the redemption side. In 1979 savings bonds redemptions were \$12.3 billion, compared to \$8.2 billion in 1978, an increase of 50 percent. Redemptions in the first quarter of 1980 were \$6.4 billion, double the amount in the first 3 months of 1979 and more than three times the redemptions in the first quarter of 1978.

Consequently, the cash loss to the Treasury from the excess of redemptions over sales in the savings bond program was \$5.3 billion in 1979, and was \$5 billion in just the first 3 months of 1980. These cash losses to the Treasury must be made up by increasing the amounts the Treasury borrows in the market, and the Treasury is currently paying significantly higher interest rates on its market borrowings. If this situation continues, it will be essential to increase the savings bond interest rate promptly in order to avoid further substantial cash drains to the Treasury and permanent damage to the savings bond program. The amount of any necessary rate increase will depend on current market conditions and on the other terms and conditions offered to savings bonds investors. We are currently reviewing the savings bonds program to determine what changes need to be made. Thus, we are requesting that the present ceiling on the savings bond interest rate be repealed as soon as possible.



Any increase in the savings bond interest rate by the Treasury would continue to be subject to the provision in existing law which requires approval of the President. Also, the Treasury would, of course, give very careful consideration to the effect of any increase in the savings bond interest rate on the flow of savings to banks and thrift institutions.

Debt limit process

I would now like to comment on the process by which the public debt limit is established.

Separate legislation for a statutory debt limit has not been an effective way for Congress to control the debt. The increase in the debt each year is simply the result of earlier decisions by Congress on the amounts of Federal spending and taxation. Consequently, the only way to control the debt is through firm control over the Federal budget. In this regard, the Congressional Budget Act of 1974 greatly improved congressional budget procedures and provided a more effective means of controlling the debt. That act requires congressional concurrent resolutions on the appropriate levels of budget outlays, receipts, and public debt. This new budget process thus assures that Congress will face up each year to the public debt consequences of its decisions on taxes and expenditures.

The Debt Limit Act of September 29, 1979, which established the current limit of \$879 billion, also amended the rules of the House of Representatives to tie the establishment of the debt limit to the congressional budget process. Under the new House rules, the Treasury still presents its debt limit requests in testimony before the House Ways and Means Committee, and that Committee makes its debt limit recommendations to the House Budget Committee. Yet, the vote by which the House adopts a budget resolution will be deemed to be a vote in favor of a joint resolution changing the statutory debt limit to the amount specified in the budget resolution. The joint resolution on the debt limit will then be transmitted to the Senate for further legislative action. No comparable procedure exists in the Senate. The Senate must still vote twice on the debt limit figure, in the budget resolution and in the separate debt limit bill. Thus, it is essential that your Committee act promptly to assure timely action by Congress on the debt limit.

*Public debt subject to limitation, fiscal year 1980, based on budget receipts of \$532 billion, budget outlays of \$569 billion, unified budget deficit of \$37 billion, off-budget outlays of \$15 billion*  
[In billions of dollars]

	Operating cash balance	Public debt subject to limit	With \$3 billion margin for contingencies
1979			
		Actual	
Sept. 28 .....	24.2	828	
Oct. 31 .....	10.5	828	
Nov. 30 .....	5.6	835	
Dec. 29 .....	15.9	846	
1980			
Jan. 31 .....	16.6	849	
Feb. 29 .....	10.7	856	
Mar. 31 .....	8.2	865	
		Estimated	
Apr. 30 .....	15.0	872	875
May 30 .....	15.0	885	888
June 30 .....	15.0	874	877
July 31 .....	15.0	879	881
Aug. 29 .....	15.0	885	888
Sept. 30 .....	15.0	881	884

*Public debt subject to limitation, fiscal year 1981, based on budget receipts of \$628 billion, budget outlays of \$612 billion, unified budget surplus of \$16 billion, off-budget outlays of \$19 billion*  
 [In billions of dollars]

	Operating cash balance	Public debt subject to limit	With \$3 billion margin for contingencies
<i>1980</i>		Estimated	
Oct. 31 .....	15	891	894
Nov. 30 .....	15	898	901
Dec. 31 .....	15	898	901
<i>1981</i>			
Jan. 30 .....	15	894	897
Feb. 27 .....	15	902	905
Mar. 31 .....	15	911	914
Apr. 30 .....	15	912	915
May 29 .....	15	914	917
June 30 .....	15	907	910
July 31 .....	15	903	906
Aug. 31 .....	15	904	907
Sept. 30 .....	15	897	900

*Federal deficits and debt, 1970-81*  
[In billions of dollars]

	1970	1971	1972	1973	1974	1975	1976	T.Q.	1977	1978	1979	1980 <sup>e</sup>	1981 <sup>e</sup>
Federal funds deficit	13.1	29.9	29.3	25.6	18.7	52.5	68.9	11.0	54.5	61.5	46.1	50.1	-2.4
Less: Trust fund surplus (+) or deficit	-10.3	-6.8	-5.9	-10.7	-14.0	-7.4	-2.4	2.0	-9.5	-12.7	-18.3	-13.6	-14.1
Equals:	2.8	23.0	23.4	14.8	4.7	45.2	66.4	13.0	45.0	48.8	27.7	36.5	-16.5
Total unified budget deficit													
Plus: Deficit of off-budget Federal entities <sup>1</sup>	-	-	-	1	1.4	8.1	7.3	1.8	8.7	10.3	12.4	15.0	18.7
Equals:	2.8	23.0	23.4	14.9	6.1	53.1	73.7	14.7	53.7	59.2	40.2	51.5	2.2
Total deficit													
Less: Nonborrowing means of financing <sup>2</sup>	2.6	-3.6	-3.9	4.4	-3.1	-2.4	9.2	3.3	-1	-1	-6.5	-12.2	-7
Equals:	5.4	19.4	19.4	19.3	3.0	50.9	82.9	18.0	53.5	59.1	33.6	39.3	1.5
Total borrowing from the public													
Plus: Change in debt held by Government agencies <sup>3</sup>	10.1	7.4	8.4	11.8	14.8	7.0	4.3	-3.5	9.2	12.2	19.7	13.6	14.1
Equals:	15.5	26.9	27.9	31.1	17.8	57.9	87.3	14.5	62.7	71.3	53.3	52.9	15.6
Change in gross Federal debt													
Less: Change in Federal agency debt	1.7	3	1.3	-2	-9	1.1	-	-2	1.4	1.4	1.6	5	6
Equals:	17.2	27.2	29.1	30.9	16.9	59.0	87.2	14.3	64.1	72.7	54.9	53.4	16.2
Change in gross public debt													
Plus: Change in other debt subject to limit <sup>4</sup>	-7	-1.2	-	-4	-	1	1	-	-	-	-	-	-
Equals:	16.5	26.0	29.1	30.5	16.9	59.0	87.3	14.3	64.1	72.7	54.9	53.4	16.1
Change in debt subject to limit													
Debt outstanding end of FY													
Gross Federal debt <sup>5</sup>	382.6	409.5	437.3	468.4	486.2	544.1	631.9	646.4	709.1	780.4	833.8	886.6	902.3
Less: Federal agency debt <sup>5</sup>	12.5	12.2	10.9	11.1	12.0	10.9	11.4	11.7	10.3	8.9	7.2	6.7	6.1
Equals:	370.1	397.3	426.4	457.3	474.2	533.2	620.4	634.7	698.8	771.5	826.5	880.0	896.1
Gross public debt													
Plus: Other debt subject to limit <sup>4</sup>	2.5	1.3	1.3	9	9	11.0	1.1	1.1	1.1	1.1	1.1	1.1	1.0
Equals:	372.6	398.6	427.8	458.3	475.2	534.2	621.6	635.8	700.0	772.7	827.6	881.0	897.1
Debt subject to limit													

<sup>e</sup> Estimate.

<sup>1</sup> Consists largely of Federal Financing Bank borrowings to finance off-budget programs.

<sup>2</sup> Largely reflects changes in the Treasury cash balance.

<sup>3</sup> Consists largely of trust fund surplus or deficit.

<sup>4</sup> Net of certain public debt not subject to limit.

<sup>5</sup> Fiscal year 1976 figure includes reclassification of \$471 million of Export-Import Bank certificates of beneficial interest from asset sales to debt.

Source: Special Analysis E, Budget of the U.S. Government.



**Exhibit 22.—Statement of Secretary Miller, April 17, 1980, before the Subcommittee on Intergovernmental Relations and Human Resources of the House Committee on Government Operations, on the President's proposal for a new revenue sharing program**

My purpose today is to discuss the President's proposal for a new revenue sharing program. The proposed bill, the Local Government Fiscal Assistance Amendments of 1980, was submitted to Congress yesterday. It expresses the President's commitment to the principle of general fiscal assistance.

The current revenue sharing program is funded through fiscal 1980 at an annual rate of \$6.9 billion. Since the program was enacted in 1972, one-third of the payments have been allocated to State governments and two-thirds to localities. The need for a balanced 1981 budget has caused the President to propose that, in the future, no revenue sharing payments be made to States. The future program would involve, therefore, only payments to local governments. These would be made at the rate of \$4.6 billion annually, which is unchanged from the present level.

As you know, inflation has accelerated during the past 2 months and the administration has redoubled its efforts to reduce it. A central element in this strengthened anti-inflation program is a revised 1981 budget—one that is balanced. To achieve that balance, the administration has reduced its originally proposed 1981 outlays by \$17.2 billion. It was necessary to eliminate funding for revenue sharing payments to State governments as part of this outlay-reduction effort. The need to cut Federal spending to reduce inflation must take precedence.

Revenue sharing payments represent about 1.1 percent of the total general revenues of State governments. The States have a far greater ability than localities to absorb a loss of this magnitude, given both their current financial condition and their legal capabilities to adjust revenues and expenditures.

However, the loss by State governments of \$2.3 billion per year in revenue sharing payments is likely to force them to cut back their own payments of aid to local governments. To assist localities, especially those experiencing the most fiscal stress, in adjusting to the reduced amounts of State aid, the President is proposing that an additional \$500 million in transitional assistance be paid to local governments in fiscal years 1981 and 1982. The likely magnitude of the impending losses in State aid to fiscally weak local governments makes such transitional assistance imperative.

**Why revenue sharing?**

Concerning our recommendations on the new program, let me put them in perspective by reviewing the history of Federal revenue sharing. The program was first enacted in 1972 to redress a fiscal mismatch. Federal taxes were perceived to be more equitable and responsive to economic growth than the taxes levied by State and local governments. At the same time, it was believed that the demands for State and local government services were rising more rapidly than the demands for the services provided by the Federal Government.

Many changes have taken place since 1972. It is no longer true that State and local—and particularly State—revenue systems are inferior. They have made major strides in broadening and refining their tax systems so that they are more equitable and more responsive to economic change.

At the same time, it is no longer clear that expenditure demands rise most rapidly at the State and local level. For instance, while the pressure for increasing education expenditures at the State and local level has eased, the aging of our population presents the Federal Government with rapidly escalating outlays for social security and medical care.

Because of these changes, the underlying rationale for revenue sharing must be reconsidered, and the program adapted to a different set of circumstances. A fiscal mismatch remains the overriding problem. But the mismatch is quite different from the one addressed by the original program.

Today the primary fiscal problem of the American Federal system is the imbalance between resources and responsibilities at the local level. Many local governments in our Nation have responsibilities for providing public services that are disproportionate to the fiscal resources to which they have access. The objective of the new revenue

sharing program must be to ensure the access of every general-purpose local government to fiscal resources in reasonable proportion to its responsibilities for providing public services.

Fiscal imbalances are due in part to the workings of our economy. In some cases, the resources of local governments are inadequate because their economies are declining or lagging behind growth in the rest of the nation as industry shifts to other areas. This problem plagues many areas of the Northeast and upper Midwest. In other cases, resources are inadequate because the locality's economy is underdeveloped. This problem is especially acute in the South and in many rural areas throughout the Nation. Neither of these reasons for inadequate fiscal resources is easily overcome by local initiatives, or even by State action. Revenue sharing is essential to enable localities whose economies are weak to provide adequate levels of public services.

Our proposals are designed to relieve the fiscal problems of the most acutely stressed local governments. This will be accomplished by improving the targeting of revenue sharing payments to local governments making an above-average tax effort and whose residents have below-average incomes. With revenue sharing relieving the most serious disparities, the States will be able to devote their energies and resources to addressing the underlying structural sources of local fiscal problems. Treasury will be monitoring the extent to which the revenue sharing program continues to assist State governments to fulfill their responsibilities for solving local fiscal problems.

### **Better targeting of revenue sharing**

The heart of the revenue sharing program is the formula that allocates funds to over 39,000 local jurisdictions. This formula is generally sound. However, our analysis over the past 2 years has established that a number of modifications are necessary to ensure that the distribution of funds makes a consistent contribution to the reduction of disparities in local fiscal capacities. We are proposing specifically that:—

1. Current procedures for distributing funds among States remain unchanged. These procedures allocate resources in accordance with general patterns of need and are based on carefully wrought compromises between a host of legitimate political interests. However, the \$500 million in transitional assistance in fiscal years 1981 and 1982 will be allocated in proportion to the current amount of aid provided by each State to its general-purpose local governments.
2. The essential logic of the intrastate distribution formula is valid and should be maintained. However, the formula should be adjusted so that higher levels of funding are directed toward full-service jurisdictions whose residents have comparatively lower incomes and bear high tax burdens.
3. The allocation procedure of the intrastate distribution should be modified so that jurisdictions of comparable size with the same incomes and tax efforts receive the same revenue sharing payments.
4. No formula modification should violate the fundamental principle that virtually every general-purpose local government in the Nation should participate in the program.

These recommendations, although modest, will significantly improve the tone of the revenue sharing program. They are based on discussions with experts in intergovernmental fiscal issues throughout the country and officials at all levels of government, a year-long review by the Office of Revenue Sharing of the available literature on the impacts of the current formula and known alternatives, and an additional year of research and development conducted by Treasury's Office of State and Local Finance.

### **The proposed allocation of local revenue sharing funds under the new program**

Let me now describe specifically the basic elements of our recommendations for a new, 5-year revenue sharing program involving \$4.6 billion in annual payments to local governments.

*Interstate distribution.* —The allocation of funds under the current program begins with an interstate allocation. Each State (not the State government) receives the higher amount of what it would receive under the 3-factor Senate formula

(population, relative income, and tax effort) or the 5-factor House, formula (population, tax effort, relative income, income tax receipts, and urbanized population). This approach reflects a compromise between regions and areas effected when the program was first approved by Congress. It is particularly important to continue these interstate allocation procedures because the sectional and regional conflicts they resolve may be even more intense today than they were in 1972.

It should be pointed out that these procedures have more to recommend them than the fact that they effectively resolve significant conflicts in our national politics. For example, the Advisory Commission on Intergovernmental Relations reports that the interstate distribution of revenue sharing funds is generally consistent with its index of fiscal stress.

*Intrastate allocation of funds.*—Once the revenue sharing funds are allocated among the States, the intrastate allocation procedure begins. The fundamental strength of the allocation of revenue sharing funds rests with this intrastate formula. The key variables of the formula—population, relative income, and tax effort—direct funds among county areas within a State and within each area in a manner that tends to reduce disparities in the fiscal capacities of local governments. In its current form, however, the capacity of the intrastate formula to contribute to fiscal equity is unduly limited in several important respects. Thus, we are proposing the following changes.

1. *De-tiering*

The current formula first allocates funds to county areas within a State and then to individual jurisdictions within each county. This tiering procedure causes some significant inequities in the allocation of funds. For example, low- and moderate-income jurisdictions in relatively wealthy counties receive substantially less funding than they would receive if they were located in a county with the same income as their own. Conversely, wealthy jurisdictions located in relatively low-income counties receive disproportionately high payments.

To eliminate these inequities, the administration proposes that the initial allocation to county areas be eliminated and that all local governments within a State compete for funds on a common basis. The result of this will be to provide all jurisdictions with the same income levels and tax efforts in a given State the same level of funding on a per capita basis.

2. *Maximum and minimum grant*

The formula now ensures each locality a per capita revenue sharing payment equal to 20 percent of the average per capita revenue sharing payment to all local governments in the same State. The formula also limits per capita grants to 145 percent of the State average. The minimum guarantees a substantial level of funding for all jurisdictions, regardless of their wealth or the scope of their responsibilities. The maximum limits the funding available to severely stressed jurisdictions; that is, those with relatively low per capita incomes and very high tax efforts.

In order to reduce the seriousness of the inequities introduced by these constraints, the administration is recommending that the minimum be lowered from 20 to 10 percent and that the maximum be raised from 145 to 175 percent. The maximum of 175 percent is appropriate because an appreciably higher limit would direct a disproportionate share of revenue sharing funds to a single large city in several States. The lower limit is appropriate because no single formula change should result in more than a 50-percent reduction in funding.

3. *Budget constraint*

Some limited-purpose jurisdictions collect very small amounts of taxes and receive little intergovernmental revenue. For such governments, the minimum-payment provision results in a revenue sharing grant that is sufficient to finance a very large proportion of their budgets. To limit these governments' dependency on revenue sharing, the current formula restricts the amount of the grant to 50 percent of a jurisdiction's total adjusted (noneducation) tax collections and intergovernmental revenues (not including revenue sharing). This provision is commonly referred to as the budget constraint. As this constraint is currently defined, revenue sharing is financing one-third of the budgets of more than 500 jurisdictions. (In contrast, revenue sharing finances less than 6 percent of the budgets of all local governments.)

As presently constituted, this provision has provided a strong incentive for the preservation of limited-purpose jurisdictions. Every increase of a dollar in local tax



revenue or intergovernmental transfers received by such a locality, if the minimum payment were not limited by the budget constraint, qualifies it for an additional 50 cents in revenue sharing funds.

Reduction of the minimum per capita payment from 20 percent to 10 percent will reduce the significance of this inequity, but no government receiving the minimum should be able to finance more than a fifth of its budget from revenue sharing. Thus, we are recommending that the budget constraint be reduced from 50 to 25 percent. This recommendation is in keeping with the principle that no single formula change should result in more than a 50-percent reduction in any locality's funding.

The reduction of the budget constraint necessitates a complementary formula change. Under the current formula, funds not allocable to a city or town because of the budget constraint are assigned to the county government that overlies the jurisdiction. If the county government is also constrained, the funds are allocated to the State government. Since State governments will no longer be eligible to receive revenue sharing, the administration is proposing that these funds be reallocated to unconstrained local governments throughout the State.

#### 4. *Scaledown for high-income jurisdictions*

From the beginning of the revenue sharing program, concern has been expressed that wealthy jurisdictions receive excessively large payments. Many very high-income communities now receive revenue sharing payments that cannot be justified by any reasonable concept of need. This is thoroughly inconsistent with the administration's view of the fundamental objectives of the program. Thus we are proposing that the revenue sharing entitlements of very high-income jurisdictions be scaled down, at a moderately more rapid rate than the current formula provides, by an amount that increases with the income level of the jurisdiction.

This can best be accomplished by the following formula modification: For each jurisdiction with a per capita income higher than 115 percent of its State's average, the jurisdiction's tax-effort factor in the formula will be reduced by somewhat more than the percentage that its per capita income exceeds 115 percent of the State average. The rationale for initiating the scaledown at 115 percent is to limit the effect of the provision to the wealthiest 10 percent of all local governments in the Nation.

#### 5. *Normalization of adjusted taxes*

The current revenue sharing formula credits several hundred relatively small jurisdictions with very high tax effort, but in actual fact their citizens are not subject to onerous tax burdens. These jurisdictions are 'tax enclaves' that export very large proportions of their taxes. In order to normalize the tax efforts of such jurisdictions, the following formula modification is proposed: The adjusted taxes included in the calculation of tax effort for a jurisdiction will be reduced by 1 dollar per capita below 250 percent of the per capita adjusted taxes of similar jurisdictions in the State (counties, cities, or towns) for each dollar that its per capita adjusted taxes exceed 250 percent of that statewide average.

This provision would not apply to a jurisdiction with per capita adjusted taxes under \$250, or to a jurisdiction that is the sole local government for its geographic area (for example, a city-county government). The \$250 limitation is designed to protect counties and townships that provide fairly high levels of services in States where the overwhelming majority of similar limitation protects jurisdictions whose taxes are high simply because they are responsible for services that are provided by two or more overlying jurisdictions elsewhere in the State.

*Overview of the impacts of the formula modifications.*—In the aggregate, the proposed formula changes will shift approximately \$200 million among local governments (less than 5 percent of total payments to localities). In terms of net impacts: Cities, Indian tribes, and rural counties realize the largest gains; urban counties experience modest losses, and townships fairly significant losses. Computer printouts detailing the consequences of the administration's proposals for every local government in the Nation have been made available to this subcommittee. The printouts include the \$500 million of transitional assistance. Allocations showing the distribution of funds in fiscal years 1983 through 1985 will be provided in the next few days.

In general, the formula changes will increase funding for large cities, and will improve the responsiveness of the allocation to variations in tax effort and per capita income. Wealthy jurisdictions will experience substantial reductions in funding.

Payments to a majority of the Nation's 105 largest county governments, typically suburban jurisdictions, will be reduced moderately; a few very high-income counties will experience large reductions. Lower income counties will experience moderate gains. Small towns and poor rural jurisdictions that offer a full range of local services will be provided additional funds.

The consequences of the formula changes vary from State to State depending on interactions between local government organization and geographical patterns or demographic structure. For example, the impacts on major cities tend to be different in the Northeast and Midwest from those in the South and Southwest. In the Northeast and Midwest, most very large cities have relatively low per capita incomes and much higher tax efforts compared with the rest of their States, and especially compared with their surrounding suburbs. As a consequence, they will experience increases in revenue sharing funding under the revised formula, often at the expense of their suburbs. In the South and Southwest, many cities have per capita incomes significantly higher than the rest of their States. Consequently, the new formula shifts revenue sharing funds from these jurisdictions to relatively poor, high-tax-effort jurisdictions, often in the rural areas of those States.

### **Compliance requirements**

Under the present program, no recipient may discriminate on the basis of race, color, national origin, sex, age, handicap, or religion in activities funded by revenue sharing. In addition, recipients must hold public hearings on their budgets to provide their residents an opportunity to comment on proposed appropriations of the revenue sharing grants. The administration recommends continuation of these compliance requirements.

Jurisdictions receiving annual payments totaling \$25,000 or more must have an audit in accordance with generally accepted auditing standards at least once every 3 years under the present program. The administration proposes to require an audit of every year's books conducted at least once every other year during the new program.

### **Transitional assistance**

The termination of revenue sharing payments to State governments, beginning in January 1981, will reduce State revenues by \$2.3 billion per year. Revenue sharing is a relatively minor component of State budgets—averaging 2 percent of their total tax receipts. Nevertheless, the loss of revenue sharing payments to State governments is likely to result in substantial reductions in the aid that the States provide to their localities.

Reliable estimates of the likely losses in State aid are not available for most individual local governments because the fiscal impact analysis necessary to identify the magnitudes of such losses has been done in only a few cases. For the same reason, estimates of the aggregate losses to all localities in each State are also unavailable. However, a recent study commissioned by the Treasury Department of the fiscal impacts of terminating revenue sharing payments to the States concludes that the total loss to local governments nationwide may be as large as \$1.4 billion.

In light of the magnitude of these potential reductions in State aid, the administration is recommending that an additional \$500 million be distributed to all local governments along with their regular revenue sharing payments in fiscal years 1981 and 1982. The objective will be to give local governments time to adjust their financial plans to the loss of State aid.

Even though estimates of direct local losses of State aid are unavailable, we expect that the losses will be most severe in States where aid to local governments is a large proportion of State government budgets. On the other hand, in States where such aid is a less important factor in State budgets, the local losses are likely to be relatively minor. Accordingly, the administration is proposing that the \$500 million in transitional assistance be allocated among the States in proportion to the amount of aid that each State government pays to its general-purpose local governments for purposes other than education. For example, if a particular State accounts for 5 percent of all State aid to general-purpose local governments in the country, that State

will receive 5 percent of the \$500 million, or an additional \$25 million in 1981 and 1982.

The transitional assistance will be added to each State's share of the \$4.6 billion in regular revenue sharing payments. The total amount allocated to a State will then be distributed among all general-purpose local governments in the State by the revised revenue sharing formula, which is discussed earlier in my testimony.

We believe that this procedure for allocating the transitional assistance will ensure (1) that the funds will be distributed to local governments in States where the loss of revenue sharing is most likely to reduce State aid to local governments, and (2) that the distribution of the payments within each State will favor the fiscally stressed local governments that are most likely to need help in adjusting to the loss of State aid.

### Conclusion

The President believes, and I believe, that through revenue sharing we can address the fiscal problems of local governments in the 1980's, and build a firm financial foundation for the future of government in America. A vital and responsive Federal system should be a national priority. But setting priorities, and finding ways to meet them, always require debate. Let us begin today a national debate on the future of American federalism.

### Exhibit 23.—Testimony of Deputy Secretary Carswell, May 1, 1980, before the Subcommittee on Agricultural Research and General Legislation of the Senate Agriculture Committee, on commodity futures markets

I welcome this opportunity to discuss the Treasury's role in the recent developments in the commodity futures markets as Treasury shares this committee's concerns about orderly markets.

The Treasury Department has no specific statutory authority over any market for commodities or any participant in those markets. As the custodian of the Nation's reserves of gold and the Cabinet agency responsible for international monetary policy, Treasury closely and continually monitors the markets for gold. Historically, Treasury was similarly concerned with the silver markets, but by 1970, silver had been eliminated from our new circulating coinage and most of the Nation's then-remaining silver reserve had been sold in the market or transferred to the General Services Administration. Treasury purchases copper for coinage and has conducted a gold auction program since May 1978, but otherwise is not directly involved in transactions relating to commodities.

In the Futures Act of 1978, the Commodity Futures Trading Commission was required to consult with Treasury prior to designation of new contract markets involving transactions of any security issued or guaranteed by the United States or any agency thereof and with respect to certain other actions. Thus Treasury's interest in financial futures is direct and tangible. However, the act did not give the Treasury any role in markets relating to commodity futures as opposed to financial futures.

Because Treasury engages in extensive monitoring of, and operations in, the foreign exchange markets, it also closely watches the markets for futures involving foreign currencies, but it has no statutory responsibility for that area.

More generally, because the Secretary of the Treasury is the chief financial officer of the Government, the Treasury Department has a keen interest in the efficient operation of all financial markets. Excessive speculation in any market that adds to inflationary pressures and expectations or which might destabilize other markets is within the purview of the Secretary. And traditionally Treasury officials have monitored markets—including the commodity markets—with those concerns in mind.

In summary, the Treasury presently has no statutory responsibility or authority to regulate the commodities futures markets, although it is a direct participant in the gold markets and has varying degrees of involvement in markets for various kinds of contracts involving future delivery.

Next, Mr. Chairman, I will address your question as to the activities of the Department relating to silver during the 6 months prior to March 27. As you will



recall, the gold market was subject to considerable speculative activity during 1979. In October 1979, then-Under Secretary Anthony Solomon met with representatives of the CFTC to discuss developments in the gold and, to a lesser degree, the silver markets. The World Bank and the International Monetary Fund had just concluded their annual meetings in Belgrade and representatives of several countries had expressed concerns about the runup of both gold and silver prices and the implications for inflation and the exchange markets. The speculative nature of trading in these markets was discussed, as well as the possible need for regulatory measures, including higher margin requirements on futures contracts for silver.

There were numerous staff contacts with representatives of the CFTC during the fall and winter, principally concerning the markets in financial futures pursuant to the statutory responsibilities I referred to earlier. It is possible that in those meetings there also may have been some discussion of the situation in silver, but I have no personal knowledge of such contacts.

My personal involvement in the silver situation commenced on the afternoon of Wednesday, March 26, when I received a call from Chairman Volcker in which he reported that a leading brokerage house might be in difficulty because the Hunt interests were failing to meet substantial margin calls. Prior to that call, I had been generally aware of speculative activity in the silver market, but I had no direct contact with either the CFTC or any other regulatory agency about this subject. In the days following March 26, I conferred frequently by telephone or in person with Chairman Volcker and the Chairmen of the Commodity Futures Trading Commission and the Securities and Exchange Commission. I did this because of the general responsibility of the Treasury to keep abreast of matters that might have the potential of destabilizing the financial markets and to take action that might be appropriate. I also conferred by telephone on numerous occasions with officials of the New York Stock Exchange and on several occasions with representatives of brokerage houses who were involved. Similarly, I discussed possible bank involvement or vulnerability with the Comptroller of the Currency, whose office is administratively part of the Treasury Department.

While in the beginning the situation was unclear, it was Secretary Miller's and my conclusion that the Treasury Department should not intervene—and we did not—with the Commodity Futures Trading Commission to recommend the suspension of trading in silver futures contracts either by the Commodity Futures Trading Commission or by any exchange or take any other overt action. Generally speaking, the purpose of the Treasury Department in following this matter so closely was to help assure that appropriate and timely action was taken by all who might have responsibilities and, if emergency action were necessary, to recommend same to the President. As I earlier stated, at no time did we conclude that the actions then being taken were deficient or that any intervention was required by the Treasury.

Finally, as requested, I would like to comment on the general issue as to whether recent events indicate that new legislation is necessary. During the past 2 years, I have testified twice before the Subcommittee on Conservation and Credit of the House of Representatives and have spoken before the Futures Industry Association about various concerns that the Treasury has about the financial futures markets and what appear to be speculative activities and tax-motivated trading therein. Those markets have grown very rapidly in the last 2 years to a point where the 3-month bill futures contract volume exceeds the cash market in that area, the level of trading now being at about \$2 trillion annually. We do not fully understand those markets and have therefore suggested that their development be carefully monitored and that new contracts not be liberally designated.

As to the commodity markets and the commodity futures markets themselves, the administration has been concerned for some time that the speculative trading in those markets may well have contributed to inflation directly and, just as importantly, to inflationary expectations. For example, precious metals accounted for about .5 percent of the 1.6-percent increase in the PPI in January. The increases feed through the production process and result in price increases in some products which are not necessarily reduced when commodity prices themselves go down. Furthermore, these price increases can result in subsequent increases in wage and price contracts tied to the price indices, further exacerbating inflation.

It is unrealistic to expect that any market will operate perfectly, but when leveraged speculation based on inflationary expectations results in extraordinarily wide swings or the fear of a corner unduly raises prices, the effect on the whole economy is unnecessarily disruptive. Hence from the overall standpoint of moderating inflation, any measures that would tend to ensure that the markets operated in an orderly and efficient fashion would be useful.

An additional concern is that when any market operates in an aberrational fashion, that can have disruptive effects in other markets. Thus if forced liquidations of positions in the commodity markets should result in bankruptcies of some participants, those bankruptcies could have ripple effects in other markets and cause significant problems. While such ripple effects have been thus far contained in the recent silver incident, the risk of their spreading is present whenever unbridled speculation results in precipitous price movements. Similarly, if the financial futures markets should operate in a prejudicial way, that could impact the cash market for Treasury securities. This is the bellwether market of our financial system and it would not be in the national interest to have that market adversely affected by speculative trading in a futures market.

Thus, in summary, it is fair to say that we in the Treasury have concern about the recent events in the commodity futures and related markets and that there may be reasons to consider legislative action. However, these are large, complex, and important markets. We do not have a complete present understanding of their interrelationships or of the jurisdictional coverage or lack of coverage by the various regulatory agencies.

Before making any legislative proposal, we believe it to be essential that the markets and the regulatory patterns be properly analyzed. Enacting ill-considered legislation could well destabilize the markets or render them less effective, just as surely as the potential excesses of the moment. Under these circumstances, the Secretary of the Treasury expects to convene a working group to address these problems and to invite participation by the various regulatory agencies. The results of the work of this group, which would also seek the benefit of views from those outside the Government, would of course be made available to the Congress and if legislative action were in order it would be proposed.

## **Economic Policy**

### **Exhibit 24.—Remarks by Secretary Miller, October 8, 1979, before the American Bankers Association, New Orleans, La., on challenges facing the economy and financial institutions**

It is a special pleasure for me to be with you this morning. Your invitation was extended to me in my role as Chairman of the Federal Reserve Board. I appreciate the opportunity to participate in my new capacity. And it is a particular privilege for me to be here in the distinguished company of the great Senator Russell Long of Louisiana and the great statesman Henry Kissinger.

#### **Challenge of change**

Your meeting here in New Orleans is being held as the decade of the 1970's draws rapidly to a close. It has been a decade marked by turbulent forces. Political and economic events of far-reaching consequences have cascaded one upon another, leaving an often breathless world to navigate uncharted waters.

In an era when change has been the norm, the pace of change has quickened. People and institutions, private and public, have been challenged to adapt rapidly or risk being left behind in the back-eddies of progress.

Your own banking industry has not been immune from these forces. On the contrary, you have faced a high order of magnitude of change, both domestic and international. The new regime of floating exchange rates, the major shifts in international balances following oil price shocks, the emergence of new credit and financial instruments both within and without the banking system, the availability of

advanced technology in communications and data processing, the increased volatility of markets, the intensification of competition, the inadequacy of savings and capital formation—these, and other developments, have presented a great challenge to the American banking system.

In the face of such dynamics, the banking industry has demonstrated remarkable resilience, flexibility, innovation, and vigor. The banker has been a person on the move, still prudent, but modern and keeping up with the times.

The challenges continue, and your agenda for action is long. Among other items, the time is ripe to phase out interest rate ceilings under Regulation Q and to authorize NOW accounts nationwide. The administration is eager to work with you to gain the necessary congressional approvals.

In particular, I want to take this opportunity to commend you of the American Bankers Association for your leadership in promoting monetary improvement legislation in this session of the Congress. The dual objectives of reducing burdens on member banks and providing greater competitive equality among financial institutions will help strengthen our banking system. The recent action of your Banking Leadership Conference in reaffirming endorsement for the concept of reserve requirements on transactions accounts of all financial intermediaries, with a lower reserve ratio below a certain deposit level, should provide momentum for favorable congressional action.

In these difficult times, I am especially encouraged by your demonstration of commitment to a strong, independent, and effective Federal Reserve System.

In like vein, we in the administration are committed to a strong and effective dual banking system. Our Nation's economic progress depends upon maintaining your strength and your vitality.

### **The threat of inflation**

Let me turn now to a broader look at our economy. Overshadowing all else is the high and persistent rate of inflation.

The causes of inflation are many and well known to you. Inflation has built up over the past 15 years. It is now deeply embedded in our economic structure. It is a clear and present danger to our national well-being.

Inflation reduces real incomes and values; it threatens our ability to provide employment opportunities; it dries up job-creating investments; it impedes productivity; it breeds recession; and it falls most heavily on those least able to bear the burden.

The war against inflation must be our top priority. There is no quick or simple solution. The war must be waged through a comprehensive strategy on all fronts on a continuous basis.

We do have an integrated strategy. We are marshalling all resources. We are directing all economic policies toward a total war against inflation.

And most of all, we are directing our efforts at the fundamental causes of inflation rather than just the symptoms.

I would like to outline the principal policies which together must form the main forces for our assault.

### **Fiscal policy**

First is a disciplined fiscal policy. The cumulative effect of large Federal deficits year after year has been to fuel the fires of inflation. We are determined to apply fiscal restraint and move as quickly as possible toward a balanced budget.

Some progress can already be reported. In 1976, the Federal deficit was 3 percent of gross national product. This year, it will be down to only 1 percent. Unless the current recession deepens, we should make further progress next year.

Even more important is to gain better control over Federal spending and to reduce the relative role of Federal expenditures in our national economy. In 1976, Federal spending was 22.6 percent of GNP. This year it will be down to about 21.5 percent. And we intend to reduce it further.

The net result, over time, of reduced deficits and reduced expenditures as a percent of GNP will be to release substantial resources for the private sector. The spending and investing decisions of individuals and businesses with respect to these resources



will be far more beneficial to our economy than channeling the same amounts through Government.

### Monetary policy

A second weapon in the war against inflation is a disciplined monetary policy. The Federal Reserve has been pursuing a course to keep firm control over the growth of the money supply. The object has been to reduce progressively the rate of growth of money and credit in order to starve out inflation.

Again, there has been some progress, and growth rates have slowed. For instance, the increase in M-1 over the past 12 months has been held to 4.9 percent—less than half the increase in consumer prices. But in recent months, following the large increase in oil prices in the second quarter, the growth has been much more rapid.

The Federal Reserve has responded promptly to counter the trend and to deal with recent evidence of renewed inflationary pressures. On Saturday evening, the Federal Reserve announced unanimous approval for a series of complementary actions. The discount rate was increased a full percent, from 11 to 12 percent; a marginal reserve requirement of 8 percent was established for managed liabilities; and the method of conducting monetary policy was revised to support the objective of containing growth in the monetary aggregates over the remainder of this year within the previously adopted ranges. In addition, the Federal Reserve Board called upon banks to avoid making loans that support speculative activity in gold, commodities, and foreign exchange markets.

These actions should serve to dampen inflationary forces and contribute to greater stability in foreign exchange markets.

### Pay price policy

Fiscal and monetary restraint represent powerful weapons to attack the fundamental causes of inflation. But they take effect with some lag. Therefore, another important policy is the voluntary program to moderate pay and price increases and thus provide time for the other basic policies to take hold.

Because of widespread cooperation, most major corporations and most labor contracts have been in compliance with the voluntary standards during the first year. As a result, overall price and pay increases have been smaller than otherwise would have been experienced.

For the second year of the program, it was felt desirable to provide for greater participation by management and labor in the process of establishing and applying pay standards. This should help avoid inequities which otherwise may develop over time. A tripartite Pay Committee, to be chaired by John Dunlop, is therefore being established, with a first task of recommending pay standards for the period ahead.

In this connection, the administration worked out a national accord with American Labor Leadership in support of the war against inflation and providing for labor involvement in the pay-price program.

### Government regulations

In battling inflation, we must not overlook the cost-raising actions of Government. Among these are the costs of unnecessary regulation. We must intensify efforts to reduce the burden of Government, and in particular the burden on the banking system.

But let me not raise false hopes. When I was at the Federal Reserve we launched Project Augeas—to undertake the herculean task of cleaning out regulatory stables that seemed somewhat like the stables of Augeas that had gone uncleaned for 30 years. The effort continues; and I hope to launch a similar attack at Treasury.

But it is not easy. Much regulation is founded in statue, and while we can improve and shorten and clarify, we often need legislation to make real reductions in burden.

So it will take time, and will need your help and support. I would particularly welcome your suggestions and recommendations in this area.

## International economic policy

Now let me turn to the international sector. A sound and stable dollar is essential if we are to achieve price stability in our domestic economy.

A declining dollar increases the prices we pay for necessary imports and otherwise contributes to higher prices here at home.

The international exchange value of the dollar is adversely affected by two basic factors: Inflation differentials with other countries and deficits in our balance of payments.

The current account position of the United States has been severely impacted by the tenfold increase in world oil prices since 1974. Consider the consequences: In 1973, this country imported \$8.5 billion of oil; this year it will be almost \$60 billion.

But despite this, we have made excellent progress toward restoring balance. In 1978, our current account showed a \$14 billion deficit. This year, the deficit will be reduced to only a few billion, even after absorbing an increase of \$16 billion in the cost of oil imports. And next year, 1980, we expect a substantial current account surplus.

In addition, we have dealt—and we will in the future deal—forcefully with unwarranted exchange market pressures. In this regard, strong measures were introduced last November 1, just a year ago. Since that time, we have achieved significant progress in strengthening the dollar exchange rate. The dollar has moved up against some currencies, down against others, and remained stable against most. Measured against the average of the major industrial countries, the dollar is now about 5 percent higher than it was a year ago. From the viewpoint of the OPEC nations, in relation to the other currencies they use to purchase their imports, the dollar has increased about 8 percent on average from a year ago.

It might also be noted that the dollar is about 25 percent higher against the Japanese yen since this time last year.

Notwithstanding favorable changes in the dollar value in terms of averages and against some currencies, we are determined to maintain exchange market stability for the dollar in terms of individual major currencies. In particular, since mid-June the dollar has been down somewhat in relation to the deutsche mark. We have therefore been giving special attention to this situation. Consultations have been held with German officials at the highest levels to assure close coordination of countermeasures.

The actions taken by the Federal Reserve over the weekend represent a positive response. By moving powerfully to assure better control over the expansion of money and credit, and to help curb excessives in commodity and other markets, the Federal Reserve will dampen inflationary forces and inflationary expectations and will contribute to greater stability in foreign exchange markets.

We will continue to monitor these markets carefully, and will be prepared to take other complementary actions when and if appropriate. We intend to maintain a sound dollar.

## Energy policy

Next is energy policy. The tenfold increase in world oil prices has been a principal contributor to the acceleration of inflation during this decade. Oil price increases have come in two major waves: The first in 1974 following the oil embargo and the second earlier this year following the upheaval in Iran.

The recent price shock has had a destabilizing effect on the world's economy. On an annual basis, the 60-percent jump in oil prices will increase the import bill of the developed countries by almost \$75 billion and the import bill of the developing countries by \$15 billion. As a result, the prospects for world economic progress are less promising. The outlook is particularly harsh for the poorest nonoil nations.

To win the war against inflation, it is absolutely essential that we reduce our dependence upon imported oil and that we reduce our dependence upon oil itself as a source of energy. The future availability and price of oil is too uncertain. We dare not risk our Nation's future on such a fragile line.

It is imperative that we establish our energy independence. It is essential to our Nation's security that we gain control over our own destiny. It is urgent that we move with all possible speed. It is vital that we pursue multiple options so as to assure total success.

For 2 ½ years President Carter has sought support for a broad and comprehensive energy program to achieve those objectives. But because we are a heterogeneous country, because some regions are producers and others are consumers, because some areas have one or another form of local energy supply and others are totally dependent on outside sources, it has been excruciatingly difficult to hammer out a national energy program.

Some important parts of the program have fallen into place earlier, such as the natural gas bill enacted a year ago. Now, remaining critical elements are under active review by the Congress.

The President has recently taken two major steps under his own powers and on his own initiative. He has decontrolled domestic crude oil prices over the next 2 years, with immediate decontrol of heavy oil. And he has limited oil imports from now through 1985 to no more than 8.5 million barrels per day, the level that prevailed in 1977. The President has established an even lower import limit of 8.2 million barrels of oil per day for this year.

The priorities for our national energy program are clear.

*First*, conservation. This is the surest, cheapest, cleanest way to reduce our dependence on oil.

*Second*, increasing the development and use of conventional domestic sources of energy, such as oil, gas, and coal.

*Third*, increasing the use of renewable energy sources such as solar, alcohol, biomass, wind, and wood.

*Fourth*, to assure longer term supplies, the rigorous development of unconventional domestic energy sources such as synthetic fuels from coal and shale and unconventional natural gas.

To provide capital resources for the overall program. A special excise tax—the windfall profits tax—has been proposed and has already passed the house. The purpose of the tax is to allocate the increased revenues generated by decontrol of domestic oil prices. A good part of the increased revenues will remain with the oil producers to provide the means for them to continue and expand production of conventional energy. Some of the increased revenues will also be allocated to the Energy Security Corporation to finance projects wholly in the private sector for the development of unconventional energy. These projects will be large-scale ventures, with unusual risks, and would not likely be undertaken by private companies on the scale needed without Government financial assistance. As an alternative, rather than seeking financing from the Energy Security Corporation, private companies will be able to take advantage of special tax credits for unconventional fuel production.

To round out the program, an Energy Mobilization Board has been proposed in order to shorten the time for obtaining permits for energy projects. We cannot afford unnecessary delays.

When fully in place, the energy program is expected to cut oil imports by more than 50 percent—4 to 5 million barrels per day—by 1990. This will put us well on the way to energy independence.

### Investment policy

Finally, a few words about capital investments. For some time, our Nation has given too much emphasis to consumption and too little emphasis to investment in productive facilities that make consumption possible.

We have fallen behind other leading industrial nations. Japan spends over 20 percent of GNP on capital investments; Germany over 15 percent. In the United States, we have been running at 10 to 11 percent. As a result, our productivity has lagged.

This must not continue, or else our competitiveness in world markets will be seriously impaired.

In coming months, therefore, we expect to be working to create conditions and incentives that will encourage the savings, investments, and productivity that are so essential to economic progress with price stability.



## Period of austerity

The war against inflation requires discipline and restraint. This means that we must be willing to accept a period of austerity for Americans—and work to see that such austerity is fairly shared—so that we will be able to achieve balanced growth with price stability in the years to come.

It is right that Government should lead the war against inflation. But the campaign will most surely succeed—and at a faster pace—if every American plays his full part. It is a time of testing for our Nation and for each of us. Your help and your support will make a great contribution toward an early victory.

## Conclusion

In considering this morning the many difficulties we face, I cannot help but reflect also on our many blessings.

Some months ago, this was brought vividly home to me. Watching the struggle of the 'boat people' to find a light in a darkened corner of the world, watching the extreme risks they endured in seeking to reach an American refuge—spoke more eloquently than I could of the living reality of the American dream.

My purpose is to do the very best I can to assure the lasting vitality of our economic system, to fight and to win the war against inflation, to reinforce the preeminence of America at home and abroad.

And to help keep alive that great American dream.

## Exhibit 25.—Testimony of Secretary Miller, October 16, 1979, before the Subcommittee on Fiscal and Intergovernmental Policy of the Joint Economic Committee, on the economic outlook, the regional impact of a recession, and countercyclical fiscal assistance

Thank you for this opportunity to discuss the economic outlook, its regional impact, and what might be done to mitigate the effects of a recession on our State and local governments. I am pleased that the subcommittee is giving its attention to this important subject.

## Economic outlook

Let me begin by summarizing briefly my assessment of the current economic outlook. In recent weeks the economy has shown more strength than earlier anticipated. Indeed GNP growth in the third quarter of this year is likely to show some recovery from the depressed levels of the second quarter. The September unemployment rate fell back to 5.8 percent after rising to 6 percent in August. Retail sales for August and September were up 5 percent in nominal terms, and almost 3 percent in real terms, from second-quarter levels. However, this strengthening of economic activity has been coupled with an acceleration of inflation, a heightening of inflationary expectations, an expansion in credit flows, and increasing evidence of speculative activity in commodity and financial markets.

In September, the rate of inflation, as measured by producers' finished goods prices, accelerated. The monthly increase of 1.4 percent was the largest single monthly advance since late 1974.

In recognition of accelerating inflationary pressures and developments in the domestic and international financial markets, on Saturday, October 6 the Federal Reserve Board acted to slow the growth in money and credit expansion.

The recent policy actions by the Federal Reserve—actions which are appropriate and necessary—will help us get a better handle on inflation, the dominant economic problem of our time. If we are to preserve the economic advances that have been made since the end of the last recession, we have no reasonable alternative but to mount a strong and broad attack on inflation and inflationary expectations.

We must recognize, however, that the underlying factors have now changed somewhat and we cannot be as certain as previously about the depth and severity of the economic slowdown. However, there are few signs that we are facing a deep

downturn of the 1973-75 type, and with economic policies focused on curbing inflationary expectations, the outlook continues to indicate a moderate recession.

The administration intends to continue its comprehensive fiscal discipline, monetary restraint, responsible pay-price policy, an overall energy program, reduction of regulatory burden, and other measures. This will contribute to a slowing of price increases during the coming months. By doing so, we can avoid an acceleration of wage and price increases and a new inflationary spiral.

By acting to slow the rate of inflation, we will be able to shore up real incomes, reduce uncertainty, reverse expectations of future inflation, strengthen consumer and business confidence, and reduce significantly the chances for a deeper recession.

The steps that have been taken to reduce inflation are necessary to restore economic stability and balanced growth. We must prove to ourselves and demonstrate to others that we have the conviction, the courage, and the fortitude to stick with the policies that are needed to bring inflation under control.

### Regional impact of recession

With this brief background on the economic outlook, let me now address the question of the regional impact of a recession.

The sensitivity of regions to a national economic recession varies widely and is dependent upon a number of factors, including industrial composition and growth rates. Historically, during periods of declining economic activity, manufacturing industries (particularly durable goods manufacturing) have tended to experience relatively wider fluctuations in output and employment than other industries. Purchases of consumer durables (such as automobiles and large household appliances) and capital goods are more readily postponed during economic slowdowns than purchases of nondurables (such as clothing and food) and many services. Thus regions which are heavily dependent upon manufacturing activity as a source of income and employment are generally more severely impacted by national recessions.

Regions that have been experiencing rapid increases in economic growth due to increased capital investment, immigration of labor, favorable climate, relatively cheap resources, or any number of other factors may be less severely affected by national economic recession than regions with slower growth rates and regions that have a relatively older, less efficient capital base. Regions heavily engaged in agriculture are not usually affected by recession to the same degree as regions heavily dependent upon industry.

During the postwar period, 1948-75, the East North Central, New England, and Mid-Atlantic States have displayed the greatest sensitivity to national economic slowdowns in terms of employment declines relative to the national average. On the other hand, the Mountain, West South Central, West North Central, and South Atlantic States have shown the least sensitivity. The degree of sensitivity is explainable basically in terms of the makeup of the economic base of the various regions.

Using the latest data then available, a 1978 Boston Federal Reserve Bank study indicates that:

(1) During the six business cycle episodes of the postwar period, employment in the East North Central, New England, and Middle Atlantic States has almost always shown percentage declines far in excess of the national average. In the 1973-75 recession, for example, total U.S. employment declined 2.9 percent from its peak to trough. Employment declined 4.7 percent, however, in the East North Central States, 4.3 percent in the New England States, and 3.8 percent in the Middle Atlantic States. Although employment declines in other regions occasionally exceeded the national average, this has been the exception rather than the rule.

In the three regions where employment declines are more severe than the nationwide average, manufacturing is the predominant source of labor and proprietor's income. Manufacturing is also more important to these three regions than to any other region in the Nation and durable manufacturing is substantially more important than nondurable manufacturing.

(2) Except for the 1969-70 recession, when employment losses in the Pacific States were aggravated by the winding down of the Vietnam war and its impact on the aerospace industry, employment declines in this region have been less than the

national average. During the last recession, the Pacific States suffered employment declines of only 1.3 percent, less than half of the national average. Although manufacturing accounts for about 25 percent of the region's total labor and proprietor's income, the relative importance of income from government, services, trade, and other nonmanufacturing sectors is greater in the Pacific region than in the Nation as a whole. Thus, the Pacific region is more diversified than many of the other regions and is less sensitive to recessions.

(3) In each of the six postwar recessions, employment declines in the Mountain States have also been substantially less than the national average. During the severe 1973-75 recession, for example, this region experienced an employment decline only half that of the national average; and in the two preceding recessions these States suffered no declines in nonagricultural employment. The Mountain States receive a smaller share of their income (less than 15 percent) from manufacturing than any other region. This fact and the fact that government and services account for larger income shares than in any other region probably assures this region of only a minimal adverse impact from recessions.

A region's industrial mix also has implications for the timing of the recession's impact. Since manufacturing activity is most sensitive to a recession, those States or regions most heavily dependent upon manufacturing (particularly durable manufacturing) generally should feel the effects of a recession first. Those States or regions also would probably be among the first to qualify for fiscal assistance from the Federal Government under the administration's proposed Intergovernmental Fiscal Assistance program that I will discuss shortly. Private forecasts of the regional impacts of the current recession seem to bear out this point.

Not all regions will be affected to the same extent by the current recession. Only those regions relatively heavily engaged in manufacturing (particularly durable goods manufacturing) or experiencing slow growth are likely to be seriously affected. In the mild 1969-70 recession, for instance, the South Atlantic, East South Central, and Mountain States experienced no declines in employment while the West South Central States showed only minimal declines. In contrast, the New England, East North Central, and Mid-Atlantic regions endured employment declines far above the national average. (Regional employment data for past recessions is presented in table 1 and regional definitions are shown in table 2.)

TABLE 1.—Percentage drop in nonagricultural employment during six postwar recessions

	United States	New England	Middle Atlantic	East North Central	West North Central	South Atlantic	East South Central	West South Central	Mountain	Pacific**
1948-49 .....	5.0	5.6	6.8	6.7	1.8	4.8	7.4	2.3	1.8	4.5
1953-54 .....	3.5	3.9	4.5	6.2	2.3	3.0	3.6	2.2	2.7	1.9
1957-58 .....	4.4	5.0	4.5	8.5	2.3	2.0	2.5	1.8	1.4	3.1
1960-61 .....	2.3	1.1	2.5	4.9	1.2	1.3	*	1.6	*	.4
1969-70 .....	1.4	3.1	2.1	4.3	1.7	*	*	.5	*	2.6
1973-75 .....	2.9	4.3	3.8	4.7	2.8	4.5	4.3	.7	1.5	1.3

\* No decline in absolute level of employment during the recession.

\*\* Data for the first three expansion periods calculated using California and Oregon employment only; data for final three periods calculated using employment figures for the entire region.

Source: Federal Reserve Bank of Boston, New England Economic Review (November/December 1978).

TABLE 2.—Census Bureau's regions of the United States

<i>New England</i>	<i>East North Central</i>	<i>West South Central</i>
Connecticut	Illinois	Arkansas
Maine	Indiana	Louisiana
Massachusetts	Michigan	Oklahoma
New Hampshire	Ohio	Texas
Rhode Island	Wisconsin	
Vermont		



<i>Middle Atlantic</i>	<i>East South Central</i>	<i>Mountain</i>
New Jersey	Alabama	Arizona
New York	Kentucky	Colorado
Pennsylvania	Mississippi	Idaho
	Tennessee	Montana
		Nevada
<i>South Atlantic</i>		New Mexico
Delaware		Utah
District of Columbia	<i>West North Central</i>	Wyoming
Florida	Iowa	
Georgia	Kansas	<i>Pacific</i>
Maryland	Minnesota	Alaska
North Carolina	Missouri	California
South Carolina	Nebraska	Hawaii
Virginia	North Dakota	Oregon
West Virginia	South Dakota	Washington

During the 1973-75 recession, the most severe economic downturn since the Great Depression, no region escaped unscathed. All suffered employment losses. Even the East South Central and South Atlantic States, which experienced no employment declines during the mild 1969-70 recession, showed large declines. At the same time, however, three regions—the West South Central, Pacific, and the West North Central States—experienced milder relative declines in employment during the last recession than they had during the mild 1969-70 recession, highlighting the fact that the regional impacts of recession differ from recession to recession.

### Studies of the regional impacts of the current recession

The administration has no official economic forecasts of individual States, local areas, or regions. However, there have been a number of private forecasts of the regional impacts of the expected current recession. Those forecasts were undertaken several months ago and are predicated upon the assumption of a modest recession for the national economy.

The private forecasts indicate that the recession's regional impact pattern will not differ greatly from that experienced during the mild 1969-70 recession.

- The New England, Middle Atlantic, and East North Central regions are expected to bear the brunt of the recession. As noted previously, all three of these regions rely heavily upon durable manufacturing for jobs and income.
- The Mountain States are expected to suffer little or no employment losses—only a slowdown in employment growth. As also noted earlier, of all the regions of the country, this one is least dependent upon manufacturing.
- The Pacific, South Atlantic, East South Central, West North Central, and West South Central States all are predicted to experience mild employment declines. Except for the Pacific region, where specific factors were operative, none of these areas experienced marked employment declines during the mild 1969-70 recession.

Of course, these studies of the regional impacts of the current recession are largely based upon historical regional impact patterns. To the extent that the weaknesses and causes underlying the current recession differ significantly from previous recessions and to the extent that structural changes in communications and transportation have taken place, the regional impact of the current recession could differ from the past.

### Current fiscal position of State and local governments

There has been considerable attention directed to the 'huge' budget surpluses enjoyed by States. However, only a few States account for most of these surpluses. More importantly, virtually all of these surpluses consist of contributions to various social insurance funds (such as retirement funds, workmen compensation, and temporary disability insurance funds) which are not generally available for other purposes. During the second quarter of this year, State and local governments actually

ran a \$6.3 billion deficit (based on national income and product accounts data) after allowances are made for contributions to social insurance funds (see table 3). This was the first such deficit since the second quarter of 1976. With the anticipated declines in the growth of employment, personal income, and retail sales due to the recession, further reductions in the rate of growth in State and local government revenues can be expected. If it were to continue for some time, such a development could jeopardize the fiscal posture of many State and local governments.

TABLE 3.—*State and local government receipts and expenditures*  
[Billions of dollars: annual rates]

	1975	1976	1977	1978	1979	
					I	II
Receipts.....	236.9	268.0	298.8	331.0	343.9	345.9
Expenditures.....	230.6	250.1	271.9	303.6	316.3	326.1
Surplus or deficit (-) (National income and product accounts).....	6.2	17.9	26.8	27.4	27.6	19.7
Social insurance funds.....	12.4	15.7	19.6	23.2	25.0	26.0
Other funds.....	-6.2	2.3	7.3	4.2	2.6	-6.3

Source: Bureau of Economic Analysis, U.S. Department of Commerce.

The spread of public sentiment for Proposition 13-type tax reductions could result in a further deterioration of the fiscal position of States and localities unless public spending is also curtailed. Curtailing public spending, however, could exacerbate the recession. A countercyclical fiscal assistance program for State and local governments would help avoid such pro-cyclical actions.

Many of the regions that will be most affected by the recession have older cities that are experiencing secularly declining economic growth rates. These cities may be particularly hard-pressed to maintain service levels in the face of the current slowdown.

The administration considered the prospects for regional variation in the effects of a recession in preparing its fiscal assistance proposal, which was submitted to the Congress last March. Let me first relate the basic justification for a countercyclical program to the evidence on varying regional effects from a recession. Then, I will summarize the provisions of the bill recently passed by the Senate, which is very similar to the administration's March proposal.

### The rationale for countercyclical fiscal assistance

During periods of economic prosperity, most States and local governments accumulate fund balances that allow them to sustain spending for as much as a year after a recession begins. At such a point, typically about the time recovery begins, fund balances have been reduced to the point where the normal spending trend can no longer be sustained, and outlays in real terms may actually begin to decline. This pattern is observable in the record of every recession and recovery since World War II, including the 1973-77 period. Although the continued growth in spending during the decline helps to reduce the seriousness of the recession, the falloff in spending tends to slow the pace of the early phase of the recovery. Thus, from the perspective of macroeconomic policy, countercyclical fiscal assistance should be triggered well after the economy has turned down. However, payments should cease after the recovery is well underway, in order to minimize potential inflationary effects.

In the current economic environment, decisions on macroeconomic policy must take serious account of the potential inflationary side-effects of any antirecession fiscal policy option under consideration. The choice among the available policy options should be based upon a careful balancing of relative job-creation effectiveness per dollar of Federal deficit against potential inflationary side-effects.

Other things equal, a policy that targets the first-round economic stimulus to areas with significant concentrations of unemployed or underutilized human and capital

resources is likely to have the least inflationary effect on prices. Such targeting cannot be achieved by traditional forms of antirecession tax cuts, which must apply uniformly throughout the Nation. However, a geographically differentiated spending program can be targeted to areas with high levels of unemployed resources.

Studies of the recent experience suggest that a countercyclical fiscal assistance program—such as antirecession fiscal assistance (ARFA) adopted in 1976 and extended in 1977, or the similar countercyclical tier of the targeted fiscal assistance program currently before the House—can be very effective in terms of job creation with minimal inflationary side-effects.

Logic and the evidence on the experience with ARFA suggest that local governments with high unemployment rates are most likely to commit such grants quickly and for job-creating purposes. This is a major reason why the targeting mechanism in the proposed program is based on local unemployment rates, rather than on such alternatives as the change in real wages and salaries.

While the recession facing the Nation is expected to be moderate, the current economic outlook remains volatile, particularly in light of the uncertainties about energy prices and availability. It therefore seems prudent to put in place a standby countercyclical fiscal assistance program such as the countercyclical tier of the Senate-approved bill that is now pending before the House Subcommittee on Intergovernmental Relations and Human Resources.

As in the administration's March proposal, there are two tiers in the Senate bill. The first involves the payment of \$85 million per quarter in targeted fiscal assistance payments in fiscal 1980 to a very small number of particularly distressed local governments.

The second tier, which is germane to this discussion today, involves a standby countercyclical fiscal assistance program which would trigger on during periods of high national unemployment rates.

#### **Standby countercyclical fiscal assistance program**

Let me indicate briefly how this countercyclical tier would work. By comparison with the 1976–78 ARFA program, the proposed program is much more highly targeted. It would only operate when the national unemployment rate reaches 6.5 percent or more for a full quarter, instead of 6 percent as under ARFA. Once the program is triggered, a recipient government would be eligible for payment under the Senate-passed bill only if its quarterly unemployment rate is at least 6 percent, instead of the 4.5 percent under ARFA. This additional targeting, in the present inflationary context, is highly desirable. It would ensure that countercyclical funds go only to areas with substantial amounts of unemployed human and physical capital, and thus are less likely to fuel inflation. Moreover, governments in areas with high unemployment rates are more likely to be experiencing significant fiscal stress, and such governments are most likely to use the payments for purposes that involve maximum job-creation effects.

The administration's mid-session economic forecast anticipated that national unemployment rates would have reached 6.5 percent or more by the last calendar quarter of 1979. This would have triggered payments under the proposed standby program. The apparent strength of the economy in the third quarter, and the events of the last few weeks, have caused us to reconsider the economic forecast, but a new one is not yet available. If the national unemployment rate reaches 6.5 percent by the first calendar quarter of 1980, this would trigger payments under the countercyclical tier, which would be distributed in the last quarter of fiscal year 1980. Given the lags in State and local budgetary processes and the spend-down of balances accumulated during the past few years, this is approximately the time when recession-induced revenue losses raise the prospect of serious budgetary disruption. This disruption will then threaten to require fiscal behavior by State and local governments that will tend to impede the early stage of the recovery from the recession.

When the program provided for in the Senate bill is triggered, it would distribute \$125 million per quarter plus an additional \$30 million for each one-tenth of 1 percent by which national unemployment exceeds 6.5 percent. One-third of the funds would be distributed to the States, the balance to eligible local governments.



## Conclusions

The proposed fiscal assistance program is an important element of the President's domestic program. It is a balanced, two-tiered program that would address the immediate needs of a limited number of fiscally strained local communities, as well as the prospective needs of State and local governments as they strive to deal with substantial economic uncertainty. In particular, the standby tier of the program is a sensible fiscal insurance program for State and local governments in the event of future excessive unemployment.

I appreciate the opportunity to discuss the pending proposals for countercyclical fiscal assistance in the context of regional variation in the economic effects of a recession. I look forward to working with you and other Members of Congress toward enactment and implementation of the program.

### **Exhibit 26.—Remarks by Secretary Miller, November 29, 1979, before the New England Council at the New Englander of the Year Awards Dinner, Boston, Mass., on a national energy program**

It is a special honor for me to receive the council's New Englander of the Year Award. In my many years as a New England businessman, I was always an admirer and supporter of the New England Council. The council has a distinguished history of service, promoting New England's economic development. You have also been an important force in developing an understanding of how national economic policies affect this area. In the energy field, for example, the council was one of the first organizations to look carefully at the issue of natural gas pricing and to demonstrate that deregulation was to New England's economic advantage.

Also, by the turn of fortune, it is very special circumstances that bring me here tonight. I have just returned from visiting Saudi Arabia, the United Arab Emirates, and Kuwait. It is appropriate that Boston be my first stop upon returning home. No section of the country relies more on petroleum than New England. No region is more affected by changes in the price and availability of oil.

Energy and inflation are the dominant economic issues of our time. It is absolutely vital that we develop a broader public understanding of what must be done with respect to these crucial matters.

In order to bring about a lasting reduction in inflation, it is essential that we have effective programs for diminishing our dependence on imported oil. My discussions with the leaders of the Arabian Gulf oil-producing nations have reinforced my conviction that we must continue to move ahead forcefully on this score if we are to avoid highly unfavorable impacts on our economy. This evening I would like to talk about our programs to accomplish this.

Our problems with energy and inflation did not develop overnight, nor will they be solved quickly or easily. Inflation has built up over the past 15 years and has now become deeply embedded in our economic structure.

The administration has, therefore, been marshalling a broad range of policies to deal with inflation's fundamental causes, not just its symptoms. We have already put into place a comprehensive anti-inflation program including monetary and fiscal restraint, voluntary price and pay moderation, balance in international payments, stability for the dollar, and major redirection of energy policies.

Taken together, these policies made up a sound strategy for defeating inflation. However, just as this strategy was becoming effective, it was overtaken by events in the energy area. The dramatic increase in energy prices following the cutback in Iran's oil production earlier this year is a primary cause of the current acceleration in inflation.

### **The impact of energy on inflation**

Energy has been accounting directly for about 3 ½ percentage points in our present 13-percent inflation rate. Its indirect impact may be another 1 or 2 percent. The energy component of the CPI has increased at an annual rate of 43 percent so far this year.

Since December, gasoline prices have risen at a 57-percent annual rate; fuel oil, so important to New England, has increased at a 67-percent annual rate. Fortunately, there was some indication last month that the rate of increase in energy prices had begun to slow.

While it is essential that we have in place all of our other programs to defeat inflation, they cannot be successful over the long run if we remain vulnerable to continued shocks from dramatic increases in oil prices. Over the longer run, the war against inflation will be won or lost on the energy issue. The danger is that another round of sharp increases in oil prices, or shortfalls in oil supply could bring higher unemployment, higher inflation, and a possible worldwide recession. For these reasons, it is of the utmost urgency that we take all steps necessary now to diminish our dependence on imported oil.

### **Restoring order to world oil markets**

The reduction in world oil production of 2 million barrels per day caused by events in Iran earlier this year was followed by speculative purchases and inventory building. This combination of events left world oil markets in perilously close balance. As a result, producers have been able to increase prices almost at will. In some cases they have done this by abrogating long-term contracts and selling a larger proportion of output in the spot market where prices have sometimes reached \$45 per barrel.

In the absence of effective efforts to conserve on energy usage, the outlook is for oil markets to remain tight next year. Free world demand for oil could still be about 51 million barrels a day in 1980. Most experts expect supply to be very close to this level. This forecast leaves little margin for comfort. A significant cutback in production by any of the major oil-exporting countries would result in serious economic disruptions. We do not expect this to happen. But as events of recent weeks indicate, we must be prepared for the unexpected.

Returning order to world energy markets will require sacrifice on the part of both consumers and producers. We have already made a start. In the International Energy Agency (IEA), and at the Tokyo summit, the major oil-consuming nations made commitments to control consumption and reduce oil imports. However, much more must be done. In the IEA, we are now working on an accelerated timetable to develop new and stronger commitments for increased reductions by member countries. If we are prepared to make the necessary sacrifices to achieve a significant reduction in oil use, the principal Arabian Gulf oil-producing countries have indicated that they are prepared to respond by producing a stable oil supply. By much cooperation between consuming countries and producing countries, we should be able to restore order to the world oil market.

The United States has made more progress than most countries in cutting back on oil imports. So far this year, we have reduced our total oil consumption by about 2.4 percent from the same period of 1978. The extent of this reduction has increased in each quarter, reaching 4.4 percent in the third quarter, despite the resumption of positive growth in our economy. Moreover, we have cut our consumption of imported oil by about 5 percent over the same period in 1978. Since the oil boycott in 1973, we have reduced by 7½ percent the amount of energy used to produce a unit of national output. While our progress to date has been good, we must do more.

### **How we became dependent on imported oil**

While the United States produces 22 percent of world economic output and has only 5 percent of world population, we account for 29 percent of world energy consumption. Not only do we consume too much energy, we also consume the wrong mix of energy. Ten years ago, oil provided about 44 percent of all of our energy. Now it provides about 50 percent. Furthermore, an increasing share of the petroleum we use is imported. In 1969, we used about 14 million barrels a day of oil, of which about one-fifth was imported. In 1973, we were using about 17 million barrels a day, of which about a third was imported. This year we will use about 19 million barrels a day, of which more than 40 percent will be imported.

The principal reason that we adopted this pattern of energy consumption is that domestic oil was cheap relative to other energy forms. For example, between 1967 and 1972 the real price of gasoline decreased by about 13 percent.

Another factor behind oil's increased share in our total energy consumption is that there were price controls on interstate sales of natural gas until they were removed last year by enactment of the Natural Gas Act. Price controls diminished the incentives for new exploration and production of natural gas. New supplies of natural gas were increasingly reserved for the unregulated intrastate market. As a result, natural gas declined from one-third of U.S. energy use in 1970 to one-quarter in 1978.

The oil embargo in 1973 and the subsequent quadrupling of the price of oil signaled the end of the era of cheap energy. This should have served as a warning of the necessity of reducing our dependence on foreign oil. Instead, we failed to respond adequately to our changed circumstances. Since the oil shock of 1973/74, two American Presidents chose to impose arbitrary price controls to keep domestic oil prices below world levels. This action has helped give the American people the false impression that oil is still plentiful and inexpensive. It is neither. While President Carter has faced the issue courageously and squarely, there are still those who fail to understand this economic reality.

Price controls encouraged the wasteful consumption of energy. They subsidized the use of domestic oil. Controls also diminished the incentive to develop domestic oil or alternate sources of energy. As a result, our total oil imports increased dramatically from 5 million barrels a day in 1973 to 8.5 million barrels a day in 1977. We have now been able to turn the tide so that in 1979 we expect to import 8 million or less barrels a day—bettering the target set by President Carter on July 15 and coming in well under the commitment made at the Tokyo summit. But we must do even more if we are to reduce our vulnerability to interruptions in the availability of foreign oil with all its implications.

Removing price controls will mean somewhat higher energy prices in the short run. However, over the longer run, pricing energy at its replacement value is essential if we are to regain control of our own destiny. That is why President Carter made the courageous decision to implement phased decontrol of domestic crude prices.

We must face economic reality. Anyone who advocates reimposing controls, and implies that we can have cheap oil, will be misleading the American people. He will simply be ignoring the consequences and the inevitable increased reliance on imported oil. Reimposing price controls on oil would place us once more on a dangerous road.

Decontrol must be an essential part of any program for U.S. energy security; but it is only a part.

The administration has proposed a comprehensive program to enable us to have less dependence on imported oil. It will require sacrifice and some change in our lifestyle, but it must be done if we are to avoid even greater difficulties in the years ahead.

The administration's program entails more vigorous conservation, and increased development of conventional energy, renewable energy sources, and synthetic fuels. Without this program, which we have been putting in place since 1977, we estimate that the United States would have needed to import about 14 million barrels a day of oil by 1990. Measures already adopted have cut that estimate to 8 to 9 million barrels a day.

When the President's latest proposals are enacted and implemented, we will need to import between 4 and 5 million barrels a day in 1990—about half our current level.

## Conservation

Conservation is the first priority in our national energy program. Conservation is the surest, cleanest, cheapest way to reduce our reliance on imported oil.

Higher oil prices in themselves will encourage more efficient use of energy. In addition, we have a wide-ranging array of tax credits, grants, financing subsidies, and other incentives to promote energy-saving investments. While some of these are just being proposed, others are already in place. The Internal Revenue Service has calculated that about 6 million 1978 tax returns claimed residential energy conservation credits totaling \$596 million.



One area in which we must do more to promote conservation is gasoline use. Forty percent of our petroleum consumption is for motor gasoline. We have established statutory requirements requiring new cars to be more fuel efficient. We are also undertaking ambitious research programs to develop more fuel-efficient automobiles. In addition, we have proposed expanded assistance for public transit.

We hope that these efforts, along with voluntary conservation by the American people, will result in a significant reduction in gasoline usage. If gasoline consumption does not decline significantly, we may have to consider new, more forceful action.

### **Increased development of conventional energy**

The second priority of our energy program is increased development of domestic sources of conventional energy. The Natural Gas Act enacted last year provided for the phased removal of controls on the wellhead price of natural gas. That action in combination with oil decontrol has substantially increased the incentive for domestic exploration and production of oil and gas.

Coal is one form of energy we have in great abundance. We are actively promoting its industrial and utility use. The National Energy Act of 1978 prohibits the use of gas or oil in new electric utility generating facilities or new industrial boilers. We are also setting targets for reduced use of oil and gas by utilities already using these fuels. We have proposed grants to help utilities make these conversions.

New England utilities, traditionally the most dependent on imported oil, are leading the way in converting to coal. Just last week the New England Electric Co. announced the conversion of its Somerset, Mass., plant to coal. Major coal conversions are also being considered for plants in Salem and Mt. Tom. Boston Edison is also exploring the possibility of building a new, 800-megawatt coal-fired plant in Weymouth, Mass.

Nuclear energy is, of course, another highly important energy source for many of our utilities, particularly in New England. The incident at Three Mile Island has demonstrated the potential perils associated with nuclear power. However, at this point, it would be unwise for us to forego the opportunities offered by the safe use of nuclear energy. The Kemeny Commission has just made important recommendations as to how nuclear energy can be made safer through more effective supervision and better training.

### **Renewable energy sources**

The first stage of our country's industrial development began in New England powered not by fossil fuels, but by water, wind, and wood. The third priority in our energy program is increased reliance on such renewable energy sources, including solar, biomass, and alcohol. While none of these sources by itself is likely to account immediately for a substantial share of our energy, together they can begin to play a very significant role today, and they will be even more important in the future. Unlike fossil fuels, renewable sources will always be available and will not pose threats to human safety or to our environment.

Gasohol, produced by mixing methanol or alcohol with gasoline, could enable us to reduce consumption of gasoline significantly. We have proposed tax incentives for alcohol used in the production of gasohol.

One of the most promising sources of energy for the future is the Sun. We are funding ambitious research efforts to develop more efficient solar devices. We also have an extensive set of incentives to encourage greater use of solar energy now, including financial assistance for the large front-end investments that are sometimes required. In addition, we also have programs to encourage the use of low head hydroelectric power. Here again, New England is a leader and already has a number of projects underway.

### **Synthetic fuels**

While the United States is running short of inexpensive, conventional oil and gas, we do have tremendous untapped resources in shale oil, unconventional natural gas, and coal. Much of this energy, however, is not in a form that can be readily used. The

fourth priority in our energy program is the development of synthetic fuels from these resources.

Over time the United States has become heavily dependent on conventional liquid fuels for transportation, heat, and power generation. However, we can no longer be sure how long we can rely on overseas suppliers to meet our needs for this form of energy. Synthetic fuels are essential as the long-term safety net to protect our economy from interruptions in the supply of imported oil.

The development of synthetic fuels will take time and require enormous financial resources. In many cases, the financial commitments required and the risks involved are greater than most private firms could assume on their own. For this reason, we have proposed an Energy Security Corporation to work with the private sector in the development of synthetic fuels. To enable it to operate with the flexibility and efficiency which this task will require, the ESC will be an independent Government agency.

### **The Energy Mobilization Board**

The regulatory requirements of Federal, State, and local governments have sometimes delayed or even acted as a deterrent to the development of important new energy sources. We cannot afford unnecessary delays in our efforts to achieve energy security. We have, therefore, proposed an Energy Mobilization board to help shorten the time required to obtain permits for new energy projects. The Energy Mobilization Board will work with State and local governments and other regulatory parties to expedite projects that are in our common interest.

### **The windfall profits tax**

The dramatic increases in world oil prices have already led to substantial increases in oil company earnings, particularly for those companies who have access to Saudi Arabian oil which has been priced at \$18 per barrel—below other OPEC oil, and far below prevailing spot prices. This lower price has not been passed on to U.S. consumers. Decontrol will generate further increases in oil company earnings. Much of this is a pure windfall, and not the result of any new economic activity on the part of the oil companies.

The windfall profits tax would use an equitable portion of the increase in oil company earnings to finance many of the energy programs so essential to our Nation's future. The tax is also essential to help pay for financial assistance to those least able to bear the burden of higher energy costs. The tax is carefully designed so that oil companies will be left with ample funds and ample incentive for the exploration and development of new energy.

The House has already passed a responsible windfall profits tax bill which meets the President's objectives and the Nation's needs. The Senate Finance Committee bill, now on the Senate floor, provides the appropriate framework, but needs to be further strengthened.

However, the Senate in action this week has further weakened the windfall profits tax by providing that each independent oil producer can exempt up to \$11 million of annual production from the tax. This exemption will cost about \$10 billion over the next 10 years while having very little impact on production.

### **Conclusion**

Recent events dramatically demonstrate the importance of immediately implementing President Carter's energy program. We must understand that time is running out. Continued reliance on imported oil leaves us vulnerable to serious economic disruptions and threatens our freedom.

We must also understand that the current levels of production are not considered by OPEC nations to be in their own self-interest. Thus, they are looking to us to exercise the discipline and self-control necessary to implement our own energy policies. If we do, I believe that we can count on their continued cooperation and constructive policies.

The greatest danger is that we do too little. We must undertake an ambitious program now. If there should be a favorable change in circumstances in the future, we can always scale back our efforts. If we proceed too timidly, we may lose forever the opportunity to reestablish American energy security.

Once the American people understand the issues involved, I am confident they will have the will to curtail dramatically their use of imported oil. The last few weeks have been frustrating and anguishing for most Americans. The most important message we can send the world right now is that we are willing to bear whatever burden and accept whatever sacrifice is necessary to recapture control of our own destiny.

**Exhibit 27.—Testimony of Secretary Miller, February 1, 1980, before the Joint Economic Committee, on the administration's 1981 budget and economic program**

I appreciate this opportunity to appear before the Joint Economic Committee to discuss the administration's 1981 budget and economic program. OMB Director McIntyre and Council of Economic Advisers Chairman Schultz will be testifying at a later date and we have submitted a joint statement for the record.

This morning I thought it might be useful to summarize briefly the administration's view of the economic situation, how the 1981 budget fits into our overall program for containing and reducing inflation, as well as to address some issues I know are of particular interest to this committee.

We have made substantial economic progress over the last 3 years. Since this administration came into office, real GNP has increased almost 12 percent, real after-tax per capita income has risen 7 ½ percent, and real after-tax profits have grown almost 15 percent. There are now 9.3 million more jobs than there were in 1976, a record of employment growth that has no parallel in the postwar period.

The most significant economic disappointment of the last few years has been inflation. At the beginning of last year it was widely expected the rate of price increase would moderate. However, just as our programs for reducing inflation were becoming effective, we were overtaken by events in the international energy market. The doubling of world oil prices was the single most important factor in the more than 13-percent increase in the Consumer Price Index last year.

Reducing inflation must be the first priority of economic policy for next year. To contain inflation now it is essential that we prevent the recent huge increases in energy prices from spilling over and becoming embedded in generalized wage and price inflation. To reduce inflation over the longer run, we must improve the structure and efficiency of our economy to restore growth in productivity—the basis for future gains in real income. The 1981 budget will help us meet these challenges.

The 1981 budget attacks inflation both by fiscal discipline and through its programmatic priorities. The growth of budget outlays is held to the lowest rates consistent with our national and economic security. The 1981 budget proposes an increase in Federal spending in real terms of only two-tenths of 1 percent. Budget outlays would be \$615.8 billion and receipts \$600 billion. The resulting \$15.8 billion deficit would be the lowest in 7 years and equivalent to only six-tenths of a percent of GNP. The 1981 budget would be balanced if it were not for the mild economic decline we are forecasting in the first half of this year.

Over the four quarters of 1980, real GNP is forecast to decrease by 1 percent; in 1981, an increase of 2.8 percent is expected. This forecast is broadly in line with many others, including that of the Congressional Budget Office. If this recession does not occur and the unemployment rate remains at the current level, the 1981 budget would be in surplus by about \$15 billion.

Fiscal discipline combined with monetary restraint will provide the macroeconomic climate necessary for containing and reducing inflation. However, in the current environment, inflation cannot be reduced by these policies alone, without enormous losses in output and employment. In addition, we must have programs designed to alleviate the underlying structural causes of inflation—in the areas of energy, productivity, investment, and government regulation. Because fundamental reforms will take time to become effective, we must also have pay and price policies to help keep inflation under control until basic improvements take hold.



The 1981 budget provides for programmatic increases in two general areas: National defense and efforts to enhance our longer run economic efficiency. The 1981 budget continues the administration's pattern of increased outlays for U.S. energy security. All of our efforts to reduce inflation will be ineffective if we remain vulnerable to continued shocks from increases in the price of imported oil. Twice in the last 10 years we have seen huge increases in OPEC oil prices. Both times the U.S. and world economy have suffered badly. During the first 4 years of this administration, spending on energy programs will have increased over 90 percent. These programs promote increased conservation as well as expanded domestic production from conventional, unconventional, and renewable energy sources.

The 1981 budget also makes provisions for addressing our underlying productivity problem through increased research and development. Over the long run, increases in productivity are dependent upon technical advances. The primary source of these advances are basic research and development. Obligations for research and development will increase by 13 percent in the 1981 budget.

The 1981 budget also contains important new initiatives to reduce structural unemployment through programs designed to prepare today's youth for the labor markets of the 1980's. While we have made tremendous advances, unemployment among some groups, particularly minority youth, remains unacceptably high. Attempting to address this problem through macroeconomic policies alone is likely to be both inflationary and ineffective. Targeted programs will help us to reduce unemployment among disadvantaged youth without inflationary consequences.

Mr. Chairman, I know that this committee is particularly interested in promoting capital formation. In last year's joint Economic Report, your committee recommended, from a longerrun perspective, the adoption of tax incentives to increase savings and investment. In particular, liberalization of depreciation allowances and other incentives were recommended to stimulate capital formation.

The 1981 budget contains no new tax incentives for investment. In our view, reductions of significant magnitude in business taxation would have been inconsistent with the basic policy of fiscal restraint that must characterize this budget. I agree, however, that as budgetary conditions permit we should consider the tax incentives that offer the greatest longrun potential for stimulating savings and investment. As you know, I have supported the concept of accelerating tax depreciation as an appropriate approach.

Mr. Chairman, let me conclude by emphasizing the importance of moving back toward budgetary balance. The administration urges the Congress to join in focusing on the fiscal discipline that is essential in order to contain and reduce inflation.

**Exhibit 28.—Statement of Secretary Miller, May 28, 1980, before the Joint Economic Committee, on the state of the economy.**

Thank you for providing me the opportunity to appear here today to discuss the current state of the economy. There have been some important developments in economic policy and performance in recent months. These hearings provide a useful and timely forum for reviewing the significance of these matters.

**The intensified anti-inflation program**

Earlier this year, while the economy was still rising, domestic financial markets came under intense pressure. In January and February, inflation began to spread beyond the energy and home financing areas. The annualized rate of inflation as measured by the CPI rose from about 13 percent during all of last year to 18 percent in January and February. Inflationary expectations intensified greatly. Serious disturbances in domestic financial markets developed in February and early March. Short-term interest rates rose by about 400 basis points, and some long-term financial markets were severely constrained.

In response to the growing threat from inflation, the President announced new actions for intensified fiscal and credit policies, reinforcing the programs of restraint already in place. The steps taken and proposed included major moves in the fiscal and

monetary areas. The administration recognized at the time that this was powerful medicine, but felt, and still feels, that it was required under the circumstances.

In the fiscal area, the fiscal 1981 budget was revised after extensive consultation with congressional leadership. The revisions eliminated some \$17 billion in programmatic expenditures, bringing the proposed budget into balance. In addition, various measures to improve tax collections and conserve energy were proposed or initiated, resulting in a net surplus for the budget. This shift toward further budgetary restraint required difficult decisions by the Congress and the administration. However, the actions were recognized as essential for national financial stability and for the long-term health of the economy.

Strong steps were also taken in the monetary area. Under the terms of the Credit Control Act of 1969, the President authorized the Federal Reserve to exercise new, temporary power to slow the growth of consumer and business borrowing. Implementation of the new measures, in conjunction with the continued exercise of monetary restraint, was remarkably successful in reversing the upward trend of credit demands and inflationary expectations. Short-term interest rates have declined by 800 basis points and more since March 14, long-term rates by more than 200 basis points, and secondary market mortgage commitment rates by about 150 to 200 basis points.

Credit and financial markets are now operating in an orderly and efficient manner. Accordingly, it has already become possible to relax somewhat the credit control measures instituted on March 14.

### The pattern of recent economic events

Since mid-March, most of the major economic statistics have indicated appreciably slower activity. It is widely recognized that the economy has entered a period of recession. The move toward recession has been quite steep, as evidenced by recent data on unemployment and industrial production. However, it is impossible to predict the whole course of the recession on the basis of 1 or 2 months of statistics. There is always an understandable tendency to assume that the future will merely reflect today's trends. That is rarely a safe assumption.

Similarly, it would be unwise to undertake basic changes of economic policy on the basis of contemporary statistics. Policy always affects the economy with a considerable lag. Most policy changes instituted now would have their major impact on the next recovery, not on the recession. This is largely the case regardless of the precise contours and duration of the downturn. It is, accordingly, very important that we keep monetary and fiscal policies on a steady course, geared to the long-term requirements of economic and financial stability. We have no cause to divert monetary policy from the objective of keeping the growth of money and credit within the established targets, or to divert fiscal policy from a dedicated, persistent effort to restrain the growth of public spending.

These considerations provide an essential frame of reference in reviewing the recent run of weak economic statistics.

- The unemployment rate rose to 6.2 percent in March and further to 7 percent in April. In April, employment fell by about 500,000, the number on layoff mounted sharply, and the percentage of industries reporting increased payroll employment hit a 5 year low. Some of the greatest employment impact has been in autos and construction, where the sharpest declines in output may now lie behind us. However, fragmentary data suggest that labor markets softened further in May.
- Retail sales in current prices have declined for 3 successive months, following a sizable increase in January. Correction to a volume basis is difficult when prices are rising so rapidly, but there has been a sharp drop in sales volume. It is well to recall that monthly retail sales data are frequently subject to large revisions. For example, upward revisions last summer removed the apparent weakness that seemed to have been developing and upon which the projections of recession at that time had come to rest. However, the current decline is more than statistical. To the extent that it reflects a temporary effect from the mid-March program, the recent Federal Reserve relaxation in the consumer credit area should prove beneficial.

- Industrial production has declined for 3 successive months and the drop of nearly 2 percent in April was the largest since early 1975. Although there are few signs of serious inventory imbalance, new orders for durable goods have weakened in recent months and further downward adjustments in production may quite possibly be in prospect.
- Housing starts averaged slightly above a 1-million-unit seasonally adjusted annual rate in March and April, down more than 40 percent from a year earlier. Building permits eased further in April, and housing starts may sink a little further before reviving. However, the decline in interest rates and increased availability of credit should begin to provide a boost for housing before too long.

### The near-term outlook

On the basis of these and other data, it is clear that the economy will register a sharp decline in real output during this second quarter. The more important question in terms of the behavior of output and employment is the pattern during the second half of the year and into next. The weight of economic opinion still expects a moderate recession. For example, four leading econometric models forecast a peak-to-trough decline in real GNP slightly greater than the average postwar recession, and substantially less severe than the 1974-75 decline.

A recent survey of 42 leading economists at major banks, corporations, and academic research organizations found the average drop expected by that group to be 2.6 percent, just about the postwar average. The administration forecast will be revised and updated in line with recent developments, and will be released in July at the time of the midsession budget review.

What are the reasons for believing that only a moderate recession is in prospect, rather than a deep decline on the 1974-75 scale? Both financial and real factors point toward a more moderate contraction.

First, in the financial area, it is important to recall that interest rates have come down very sharply from their earlier peaks. Savings flows to thrift institutions have picked up recently and the financial preconditions for an upturn in housing are already being established. A general increase in credit availability and lower interest rates will also provide support for those sectors of the economy that depend heavily upon consumer credit and business borrowing. In the process, the heavy burden that has come to rest upon small- and medium-sized business and agricultural borrowers should gradually be removed.

Second, in the nonfinancial area, there are still no signs of serious inventory imbalance, and inventory-sales ratios remain at relatively low levels by past standards. Difficulties in correcting for inflation can leave some doubt on that score in terms of inventory volume, particularly in some areas of manufacturing. Still, there is nothing visible to this point which suggests that inventory accumulation is generally excessive. Indeed, cautious inventory policy is one reason why output has fallen so sharply in the current quarter in response to sales declines. In some past recessions, production has continued in the face of a pileup of inventories which only makes the eventual adjustment worse.

Plant and equipment spending plans have continued to show encouraging strength, although it is only realistic to suppose that some modest softening may soon begin to appear. In general, however, businesses are taking a longer view and building the modernization improvements and additions to capacity that will be needed out further in the decade, well beyond the current adjustment.

It seems quite probable, therefore, that the economy is already experiencing its sharpest fall during the current quarter. During the balance of the year, some positive factors should begin to emerge in areas of the greatest current weakness. Auto, housing, and construction activity will not continue to decline at recent rates. Instead, these important sectors of activity are expected to bottom out and begin to post some gains in a lower interest rate environment. It is our best current judgment that the recent drop in the economy will not cumulate much further. Of course, no one can state that with complete certainty. But, on the basis of the information in hand and apparent trends, a modest further decline after the current quarter appears to be the



most probable outcome. Needless to say, the current situation is being monitored carefully.

### The inflation problem

Inflation is, and must remain, our number-one priority. Already, in the wake of the March 14 measures, there are encouraging signs. The dramatic decline in interest rates in the past 2 months signals an abrupt drop in inflationary expectations, as well as a softening economy. Sensitive materials prices have fallen sharply in March and April, which also signals a favorable turn in the inflationary process. Because of lags in the process, full results cannot be expected to show through immediately at the later stages of the productive process. However, the consumer price results in April were encouraging, with the lowest monthly increase in more than a year. Admittedly, the favorable Producer Price Index result in April was heavily influenced by falling prices of food and farm products which will not continue on that scale. But there are pervasive signs that the inflation outlook is in the early stages of significant improvement. In May, the members of the National Association of Purchasing Management reported the lowest rate of price increase in 3 years. This may be the leading edge of things to come in the important area of industrial prices.

There is a dependable and predictable cyclical sequence in costs and prices. It can be seen in every postwar recession and we are beginning to see it now. First, the rate of economic expansion tapers. Second, sensitive industrial material prices begin to fall. Third, after some lag in time, lower rates of inflation are experienced at the final stages of the production process. The first two stages—a softer economy and declines in sensitive prices—are now clearly visible, and the third stage—lower rates of inflation at the consumer level—will become increasingly evident as the year progresses.

The problem is that although every postwar recession has lowered the existing rate of inflation, every expansion in the past two decades has then lifted the inflation rate to a new higher level. This successive ratcheting up of the rate of inflation must be reversed in the interest of longrun economic stability. The fiscal and monetary decisions we make now will be affecting the inflation outlook for some time to come. It is widely felt—here and abroad—that we stand at a crossroads so far as inflation is concerned.

Thus we must not be diverted from our objective of combating inflation, and be tempted into a policy of excessive economic stimulus. Any premature relaxation of the basic policies of restraint could whipsaw the economy and financial markets. Interest rates and the rate of inflation could easily be driven back up again, with serious consequences for auto production, housing construction, and the entire economy. Instead, the proper course to follow is one of continued discipline, to ensure progress in reducing the rate of inflation.

### The budget and tax cuts

The key to the current situation is maintaining close control over Federal spending. That now lies well within the reach of the Congress, and you and your colleagues deserve full public support in this crucial effort. If the economy runs close to the path projected in late March and Federal spending is tightly controlled, the proposed budget would show a surplus. Even if the recession is somewhat worse than forecast, the budget proposed by the administration could still be in balance. In any event, in the present situation, with inflation still deeply embedded in the economy, it is essential to maintain discipline by controlling Federal spending.

Most importantly, the steps that were taken on March 14 must be seen as a crucial element of longer term efforts to bring the growth of Federal spending under control. During the 1970's, we have had continuous budget deficits in both good times and bad. If we are to improve productivity and bring inflation under control, the Federal Government cannot continue to place ever-escalating demands on the economy and capital markets. It is essential that we return a larger share of our national output to the private sector where it can be more effectively utilized.

It is far too soon to be talking of tax cuts. Instead, we need to demonstrate our ability through the legislative process to bring expenditures under control. Tax cuts purely for the purpose of economic stimulus and attempted quick fixes for the

economy are not appropriate in the current situation. Instead, any tax cuts need to be preceded by clear progress in reducing the rate of growth in Federal spending, and justified on the basis of their contribution to longer range goals of productive efficiency and lower inflation rates.

In recent years, this committee has played an extremely important role in directing attention to the need for a different approach to the economic problems of the 1980's. More emphasis does need to be placed on productive efficiency—the supply-side approach in the current terminology. Greater incentives do need to be offered for saving and investment, and less for immediate consumption. Therefore, we must carefully chart our near-term course in the fiscal area. Otherwise, the latitude required for sensible fiscal action to deal with the deep-seated problems of productivity and capital formation could be frittered away through a piecemeal process of tax reduction to encourage consumption.

Our tax system has important effects on our economy, and many of the so-called supply-side effects have been unduly neglected in the past. Research in the last few years has sought to address this omission, but the real value of such research becomes evident only when it is integrated into a coherent view of the economy as a whole. Tax cuts affect aggregate demand as well as the composition and growth of "aggregate supply." If we are to fight inflation as well as increase productivity growth, both sides of this equation must be taken into consideration.

### Conclusion

The need at the present time is to demonstrate our resolve to deal with the inflation problem. What is required is consistency and persistence, coupled with a readiness to adapt sound economic policies to changing economic circumstances. That readiness was demonstrated at mid-March and subsequently. The task remaining is to follow through with steady policies that will guide the economy onto a less inflationary long-term path.

### Exhibit 29.—Statement of Secretary Miller, September 9, 1980, before the House Budget Committee, on the President's proposed economic revitalization program

Thank you for giving me the opportunity to discuss with you the economic revitalization program that has been proposed by the President. The program is the product of careful deliberation as well as consultation with the Congress and the public. Our economic problems are longstanding in nature and they will not be solved overnight. But this program represents an important step to healthy economic growth during the decade of the 1980's and beyond.

The President's program will help reinforce the imminent recovery from the current recession, the seventh in the postwar period. However, the program is not a traditional stimulus package, but rather is designed to help us meet the long-term challenges facing our economy.

The importance of following such a course is clear. Traditional stimulus programs have almost always been enacted too late in the business cycle; rather than cushioning the fall in the economy they have accelerated inflation during the ensuing recovery. Difficulties in forecasting the exact timing of economic change as well as the time needed for legislative changes have made this process almost inevitable.

While the fall in national output in the second quarter of this year was very steep, a wide range of statistics suggests that most of the decline is now behind us and that this recession may be one of the shortest in history. Much of the current recession has been concentrated in the automobile and housing industries. Aided by falling interest rates, there are signs of recovery in both of these sectors. Consumer spending has also risen significantly in recent months. Manufacturers' new orders have increased sharply after a period of decline. Labor markets are beginning to stabilize and the unemployment rate actually declined slightly in August. The index of leading economic indicators rose very sharply in the last 2 months.

While natural healing forces are building a base for recovery from this recession, inflation is still too high and many of the longer term problems facing our economy must still be addressed.

The program the President announced on August 28 will address these problems and is a strong first step toward building an even more vital economy.

### AN ECONOMIC PROGRAM FOR THE 1980's

The administration's economic program for the 1980's will encompass comprehensive policies directed at our principal objectives:

- To reinforce recovery from the current recession and put people back to work in productive jobs.
- To revitalize American industry, working in partnership with business, labor, and the public.
- To increase substantially the share of national output devoted to investment in order to create jobs, encourage innovation, and improve productivity.
- To continue the war against inflation so the gains from industrial growth are not eroded.
- To implement our national energy policy of reducing oil dependence so that more of our workers' dollars will stay at home.
- To maintain a sound and stable dollar which contributes to world economic and financial stability and growth.

### INDUSTRIAL REVITALIZATION

Revitalizing American industry to provide even stronger growth in jobs and national income in the 1980's will require a new spirit of cooperation among business, labor, and Government.

A great strength of the American economy is its primary reliance on the private enterprise system. The cumulative effect of millions of decisions by individuals and businesses within a competitive marketplace is by far the most effective and efficient way to provide for our Nation's needs and wants. However, private industry and workers in America face the challenge of unprecedented change.

The economic world of the 1980's is vastly more complex than that of the 1950's and the 1960's. We have become more heavily involved in international trade, and forces influencing the international competitiveness of our industries have taken on increased importance. The pace of technological change has accelerated, creating opportunities but necessitating adjustment. The character of American industry and the work skills it needs are changing. Actions of government at the Federal, State, and local levels increasingly affect our industries.

The role of the Federal Government in seeking to revitalize American industry is primarily to create a climate which encourages private innovation and investment and creates permanent and productive private sector jobs. In present circumstances, because of the speed and scale of change in the Nation's industrial structure, Government must go further. It should also help smooth the adjustment process of communities and workers to avoid undue distress and hardship.

#### Encouraging cooperative efforts

*The President's Economic Revitalization Board.*—To reinforce cooperation between Government and the private sector in dealing with the complex issues of industrial policy, the President will establish a new, high-level Economic Revitalization Board, comprised of representatives of industry, labor, and the public. The board will advise the President on the broad range of issues involved in the on-going process of revitalization.

The board will be requested to develop specific recommendations to the President for establishment of an industrial development authority to provide financial assistance for industrial development and economic revitalization in areas in transition and affected by industrial dislocation or high unemployment, or if needed to remove industrial bottlenecks.

The authority would mobilize both public and private resources such as Federal, State, and local monies and capital from private markets and pension funds. Its



programs would be coordinated with State and local development functions. The authority would be subject to annual budget control.

The President will seek the board's advice on other matters, including:

- Providing guidance on improving the skills of the American workers to meet the needs of the coming decade.
- Recommending ways the social goals of regulations can be accomplished while minimizing compliance costs and maximizing productivity of industry.
- Dealing with the impact of industrial dislocation on workers and communities.

This extensive mandate to work with the administration on major policy issues on a sustained basis is appropriate in view of the intricate and interdependent relationship among Government, labor, and business.

### Encouraging private capital investment

Substantial gains in our standard of living depend on strong and continuous growth in productivity. Our productivity growth, however, has slowed seriously over the last decade. Insufficient capital investment is an important cause of this disappointing trend.

To improve productivity, as well as to provide for the energy resources necessary for our economic and national security, will require that an increased share of our national output be devoted to investment. To accomplish this, the administration will propose tax changes to encourage investment.

*Liberalized depreciation.*—A new system of depreciation allowance, the amounts a business may deduct from its income to recapture its capital investment costs, will be proposed for enactment next year, effective January 1, 1981. Liberalized depreciation allowances will encourage business to expand investment, to modernize productive capacity and to provide new jobs. The depreciation program will be designed:—

- To provide for a constant annual rate of depreciation for each asset class.
- To reduce the number of asset and industry classes to 30 or less from the present 130. Few taxpayers would use more than 2 or 3 classes.
- To simplify the procedures for using accelerated depreciation.
- To increase the allowable depreciation rate by approximately 40 percent.
- To allow roughly equal liberalization of depreciation for all assets, thus minimizing economic distortions.
- To take effect immediately upon the specified effective date, thus avoiding complicated transition rules that tend to delay some investments.

The constant rate depreciation system will reduce tax revenues by an estimated \$6.3 billion in the first year, increasing to \$24.2 billion by 1985.

*Refundable investment tax credit.*—To help industry obtain capital for investment in new plants and equipment, the tax code permits a 10 percent investment tax credit against the first \$25,000 of tax liability and against 90 percent of the remainder (80 percent in 1981).

Since this investment incentive is in the form of a tax credit, it offers no current benefit to industries with either limited or no tax liability. Thus, it is of little or no immediate value to firms suffering temporary losses or reduced profits. The present investment credit is also effectively denied, at least in part, to new firms just starting out which have not yet produced taxable earnings. These enterprises are often an important source of technological progress and innovation.

As part of its program, the administration will propose that 30 percent of the earned but unused investment tax credit be made refundable beginning in 1981. The portion of the credit not made refundable will be available for carryback or carryforward as under present law.

It is estimated that the first year cost will be \$2.4 billion, and the fifth year cost \$2.3 billion.

### Reducing employer payroll taxes

Liberalized depreciation allowances and a partially refundable investment credit will reduce industry's capital costs and encourage investment. The administration will also propose measures to reduce labor costs and further encourage employment. The social security tax increase for employers scheduled to take effect in 1981 is essential to maintaining the system's financial integrity, but it adds to labor costs and thus to inflation. This increase would be particularly burdensome on those businesses which rely more heavily on labor than on machinery.

The social security credit will be in effect for 2 years beginning in 1981. This will allow time to consider the broader issues of social security financing. The first-year revenue cost is estimated at \$6.6 billion.

*Aiding small business.*—The administration is particularly interested in small business because it is a prime source of innovation, provides a large share of the growth in jobs each year, and includes many minority entrepreneurs. Liberalized and simplified depreciation allowances and the refundable investment tax credit are of particular value to small business. In the past, the complexities and recordkeeping requirements of accelerated depreciation have effectively denied this incentive to many small businesses. The administration's proposal greatly simplifies the depreciation system and substantially reduces recordkeeping requirements. The refundable investment tax credit will be beneficial to newly established companies during the startup period when they have not yet generated taxable earnings. Since many small businesses rely more heavily on labor than machinery, the employer social security tax credit also will be particularly beneficial to them.

The administration will also propose changes in the tax code that will allow new businesses to write off most startup costs, and recommend liberalizing Subchapter S requirements to enable more investors to participate in new ventures. The administration's support of the Regulatory Flexibility Act reflects its continued commitment to reduce regulatory burdens on businesses, and particularly on smaller companies.

### Assistance to distressed areas

While private capital and its allocation through the marketplace is the basis of the administration's revitalization program, more encouragement of private investment and public development capital is needed for industrial renewal in areas undergoing economic transition.

*Increased economic development funding.*—The Carter administration has substantially increased Government support for economic development. In FY 1980, overall economic development programs are funded at more than \$3.5 billion, 70 percent above the level when the administration came into office. This includes the administration's new \$675 million urban development action grant program to stimulate private investment in distressed areas. In addition, funding for programs to aid small business has almost doubled. Further, the Congress now has before it the administration's proposal to increase the Economic Development Administration's program level from \$600 million in FY 1980 to \$1.7 billion in FY 1981. The administration urges prompt enactment of the proposed EDA legislation.

To enhance existing public efforts and meet expanded needs, next year the President will propose additional program levels of \$1 billion for FY 1981 and \$2 billion for FY 1982 for economic and industrial development programs.

*Targeted investment tax credit.*—As a supplement to ongoing programs designed to foster growth in economically distressed areas, the administration will propose a special targeted investment tax credit of 10 percent for eligible investment projects in localities of high unemployment.

It is estimated that the revenue cost will be \$200 million in the first year and an average of \$800 million a year through 1985.

### Investment in energy security

Continued progress in the energy area is an essential part of the administration's economic program. Enormous investments in conservation and domestic energy production are required over the next decade to accomplish the reduction in oil

imports so essential to our national and economic security. These investments will create hundreds of thousands of jobs domestically and will help protect the jobs of all Americans from future oil price shocks.

Through phased decontrol and the other measures already undertaken, America has reduced its oil imports by about 20 percent from their previous peak levels. Most importantly, this reduction has been the result primarily of increased conservation and use of domestic energy resources and not lower economic activity. The amount of energy required per unit of output has been substantially reduced.

Together with Congress, the administration has provided for vastly increased funding for energy conservation and production since 1977. In addition to appropriations for the Synthetic Fuels Corporation, the 1980 budget provides about \$5 billion for energy production and conservation, more than twice the level when the administration took office.

Over the last 4 years, to stimulate production and conservation, Congress has approved tax credits which will provide \$4 billion in benefits by the end of FY 1981. In addition, \$20 billion (out of an ultimate \$88 billion) in budgetary authority has been appropriated for the Synthetic Fuels Corporation to assist the private sector in creating a major new synthetic fuels industry. The goal is for synthetic fuels to supply about 2 million barrels of oil per day by 1992.

The 1981 budget provides for even greater funding for energy conservation and production. The administration has proposed to the Congress a \$10 billion program to help finance electric utility conversion from oil to coal or other fuels. This program will save an additional 500,000 barrels of oil per day by 1990.

The Congress also has before it our proposal to create an Energy Mobilization Board to help expedite the administrative process in establishing energy-related facilities.

Both of these pending bills need to be enacted by Congress as soon as possible.

The administration will propose in January an additional \$1.2 billion over 2 years for energy conservation, including increased funding for the Solar and Energy Conservation Bank, conservation investments in federally owned public housing units, improvements in the efficiency of federally owned power plants, and weatherization of schools and hospitals and low-income housing units throughout the United States.

### **Research and technological development**

Technological advance and innovation have accounted for much of the productivity growth in the United States in the past half century. They are essential elements of economic vitality.

In cooperation with Congress, the Carter administration has increased obligations for research and development from \$26.2 billion in FY 1978 to \$35.4 billion in FY 1981. Basic research spending increased by about 35 percent in the same period, from \$3.6 to \$4.9 billion. In addition, the administration has stimulated new research programs between industry and universities, encouraged Government-industry cooperation; for example, in the automotive sector, and has increased support of smaller high technology firms.

As part of the economic revitalization program, and beyond the fiscal proposals aimed at stimulating investment and innovation, the President will propose in January an additional \$600 million in budget authority for fiscal years 1981 and 1982 to stimulate research and technological development. With this commitment, funds for basic research will grow in real terms by 3 percent per year.

### **Export promotion**

In the past 10 years, the share of the American economy devoted to exports has almost doubled from 6.4 percent in 1970 to over 12 percent in the first half of 1980. Foreign markets have become increasingly important for American firms. When President Carter took office, exports of goods accounted for about 6.7 percent of GNP; this year they will account for about 9 percent. In dollar terms, exports of manufactured items have grown by 75 percent. This increase in exports has been an essential source of jobs and of revenues needed to pay for oil and other imports.



This administration will continue to stress the growth of U.S. exports. To do this it has already increased support of the Export-Import Bank more than sevenfold over the last 4 years, and it has reorganized and combined the Government programs which support U.S. international trade.

In addition, the administration has supported Export Trading Company legislation now in Congress that will encourage small and midsize business participation in export markets. In January, we will propose an amendment to the Internal Revenue Code to provide for an exclusion for income earned abroad in certain areas. This is designed to help improve the ability of U.S. firms to sell and service products abroad.

### **Developing economic infrastructure**

*Transportation.*—The ability to transport people and goods efficiently is essential to our economic, energy, and national security objectives. Since the beginning of this administration, Federal funding for transportation has increased by 96 percent. We must continue to make substantial investments in all areas of transportation. For example, Congress now has before it a 5-year program amounting to \$25 billion for mass transit facilities, \$6.1 billion for airports and the airway system, and \$1.5 billion to assist in restructuring the Nation's railroad system, particularly in the Middle West. Improvements to the northeast rail corridor totaling \$2.5 billion are already underway.

Our national highway system is an integral part of our transportation system and has been constructed over many years at great expense. Evidence is mounting, however, that more investment is needed to maintain this vital national asset. The 1981 budget contains \$8.4 billion to complete and repair the Federal highway system, including \$950 million for rehabilitation of bridges.

The administration will propose a \$600 million increase in FY 1981 transportation obligations to deal with additional needs of the highway system and other forms of transportation.

*Coal.*—The United States has enormous deposits of coal, and there is a great opportunity to expand the use of this energy resource both at home and abroad. Coal will be an important new export product for the United States. Bottlenecks in our coal transportation system, particularly at seaports, however, are a serious impediment to expanding the use of this abundant natural resource.

Port facilities for coal exports need modernization and enlargement. While much of the investment will come from private sources, the Federal Government will play a role in deepening ship channels to accommodate larger and more efficient coal-carrying vessels. The President has asked the Army Corps of Engineers and other Federal agencies to expedite all aspects of their review of coal port projects.

### **Regulatory reform**

Health, safety, and a clean environment are important national goals, just as are economic growth, stable prices, energy self-sufficiency, social justice, and national security. Some of these goals conflict with one another, and all compete for resources. Choosing the policy that achieves the best balance among these conflicting and competing goals is a difficult task.

Regulatory reform is an important element in policies to promote healthy economic growth and to improve productivity. The President continues to call for passage of the Regulatory Reform Act and the Regulatory Flexibility Act.

Over the past 3 years, the Carter administration has taken major steps in regulatory reform. We will build on that foundation and attempt to reduce still further the dead weight of unnecessary Government regulatory interference.

### **ASSISTANCE TO PEOPLE AND COMMUNITIES**

The economic changes taking place around the world create special problems for many people and communities. The Federal Government must play a part in helping to ease the burden of adjustment for those affected adversely. The changes also provide increased opportunities. Government must facilitate the training, retraining, and education of Americans for jobs in the industries of the 1980's.

### **Proposed extension of unemployment benefits**

Our unemployment compensation system is an essential form of assistance to workers who have lost their jobs. The President is proposing a temporary unemployment compensation program so that workers suffering long-term unemployment in this recession will be eligible for benefit payments for an additional 13 weeks.

### **Human resources**

The more than eight million jobs created during the Carter administration—the largest growth in employment over any similar period in our history—are the product of both private and public initiative. Federal funding for employment and training has expanded from \$6.3 billion when this administration took office to about \$10.4 billion in FY 1980. Federal spending for basic and vocational education expanded from \$4.7 billion in 1976 to \$7.3 billion in FY 1980. In 1981, the Vocational Education Act will be up for renewal. The administration will be continuing a major effort to prepare our citizens for employment.

*Adjustment and training programs.*—The trade adjustment assistance program provides benefits, job training, and relocation to workers who have been adversely affected by imports. Currently, 310,000 auto workers are eligible for benefits in addition to 134,000 workers in other adversely affected industries. FY 1980 benefit outlays to date amount to about \$1 billion.

The administration is also working to devise better means of retraining and relocating workers displaced by industrial changes. The President has proposed broadening the trade adjustment assistance program to supplier industries to make sure that all workers receive its protection. A series of special demonstration projects, under the Department of Labor, will be launched to assess the merits of different methods for retraining and relocating displaced workers. One such project is already underway in Michigan.

The administration has established two public services employment programs under CETA which now provide 400,000 jobs. Welfare reform demonstration projects in 12 sites around the country are enrolling welfare recipients in employment activities which will ultimately lead to another approximately 400,000 job opportunities. In addition, CETA presently spends over \$2 billion on programs designed to prepare the disadvantaged for jobs.

The President will request an additional \$300 million in FY 1981 for training under CETA to provide job opportunities for the disadvantaged and the unemployed. The program will be based on the experience of the present network of employment and training programs, but will require special efforts to identify jobs in emerging sectors of the economy.

The administration recognizes the paramount importance of private sector permanent jobs and the essential role of the private sector in providing job training and employment. The private sector initiative program, funded at \$400 million during FY 1980, directly involves business and labor in training activities. Private Industry Councils, composed of a cross section of local communities, have been organized with virtually every CETA prime sponsor throughout the country. In addition, the targeted job tax credit provides incentives for private employers to hire economically disadvantaged persons. The goal this year is 215,000 job placements.

*Youth employment.*—Youth represent one of our most vital natural resources. Expenditures on youth training and employment have expanded from less than \$2.5 billion in 1977 to over \$4 billion today.

Young people must develop basic job skills to participate in the economy's growth. The President has proposed a \$2 billion 2-year youth initiative, pending before the Congress. The initiative draws together programs in the Departments of Labor and Education to assist disadvantaged youth in breaking free from idleness and poverty. The program needs to be enacted promptly.

### **Countercyclical revenue sharing**

Because of the scale of change, some communities undergoing economic transition will require financial assistance to help maintain local services. Increased countercyclical

cal revenue sharing will help assure that harmful temporary reductions in service levels do not take place. The Congress is considering countercyclical aid to cities and communities. The President will work with the Congress to enact a \$1 billion countercyclical revenue sharing program for FY 1981.

## REDUCING INDIVIDUAL TAX BURDENS

### Offsetting social security tax increase

Inflation has reduced the real disposable income of American workers both by diminishing their purchasing power and increasing their tax burdens. But general tax cuts that result in a greatly expanded Federal deficit and reignite inflation are not of lasting benefit to Americans.

The social security tax increase scheduled to take effect in 1981 will increase tax burdens on individuals and retard the recovery of consumer purchases. While the revenues from that social security tax increase are necessary to assure the financial soundness of the social security system, the increased tax burden on workers is best offset by carefully targeted reductions in income taxes.

The President plans to accomplish this objective through a social security income tax credit for individuals to be proposed in January. It will be available to all individual taxpayers and will consist of a nonrefundable credit against Federal income taxes equal to 8 percent of the social security taxes paid. The credit will be in effect for 2 years beginning in 1981, thus allowing time in which to consider the broader issues of social security financing. The first-year revenue cost is estimated at \$6.2 billion.

### Earned income tax credit

The President will also propose liberalization of the present earned income tax credit in order to provide relief for nontaxable people with dependent children. Under current law, individuals with dependent children may claim a refundable earned income credit equal to 10 percent of the first \$5,000 of earnings. The credit phases out as income increases from \$6,000 to \$10,000. The Administration will propose raising the credit from 10 percent to 12 percent, while increasing the phase-out to \$7,000 to \$11,000. The first-year cost is estimated to be \$900 million.

### Reducing the marriage tax penalty

The marriage penalty is another tax burden that needs to be addressed. Families with two wage earners may owe higher income taxes than would be the case if the spouses were unmarried individuals. The President will propose a tax deduction equal to 10 percent of the lower earning spouse's earnings up to a limit of \$30,000. The first-year revenue cost is estimated at \$4.7 million, rising to \$8.9 billion in the fifth year.

## ANTI-INFLATIONARY FISCAL AND INCOMES POLICIES

The acceleration in productivity growth that results from the measures proposed by the President will slow the rise in business costs and thereby lead to lower inflation. As the President's energy programs are carried out, the Nation's dependence on foreign oil and its vulnerability to inflationary external shocks will be reduced.

But these inflation-lowering consequences of the administration's economic program will take effect gradually. And they are not sufficient, taken alone, to accomplish the tasks of preventing the reemergence of inflationary pressures and of steadily lowering the inflation rate.

*Budget policy.*—Measures to increase supply, raise productivity and improve our energy security must be undertaken within the framework of prudent and cautious budgetary policies. The administration wants to speed recovery. It does not want, however, to risk a renewal of inflationary pressures and invite a resurgence of sharp increases in interest rates.

- That is why the President has insisted that a tax cut prior to the election is unacceptable. A tax bill, developed, debated, and passed in a few weeks, during the heat of an election campaign, is certain to be incompatible, in both size and design, with anti-inflationary objectives.



- That is why the measures in this program have been rigorously screened to ensure that Federal spending is not increased by a dollar more than is needed to meet the Nation's goals for industrial modernization, energy security, and smoothing the path of economic adjustments.
- That is why the President strongly opposes proposals which have been made for a schedule of massive tax reductions in 1981 and subsequent years that would guarantee huge and inflationary budget deficits.
- That is why the President decided to propose reduction of tax burdens through a credit against social security payroll taxes, since this approach cuts employer payroll costs and thereby contributes to lower prices.

Taken together, the tax and spending measures recommended by the President will reduce revenues by some \$27.5 billion in calendar year 1981 before taking into account the offsetting revenue gains from higher economic activity. This gross revenue loss would rise to an estimated \$58 billion by 1985. In 1981, and even more strikingly in later years, the revenue losses from these tax measures are substantially less than those contained in other tax proposals which have been prominently mentioned in recent weeks and months. With the President's measures, outlays will be increased by about \$2 billion in fiscal 1981 and by about the same amount in fiscal 1982.

Because the recommended program will increase economic activity and taxable income, the net loss of Federal revenues will be smaller than the numbers cited above. Some savings in unemployment compensation payments, and other outlays relative to the level of unemployment, will also occur. Moreover, the tax reductions and other programs will not become effective until the fiscal year is already well underway. As a consequence, the measures proposed in the President's overall program will increase the 1981 budget deficit by \$6.0 to \$7.5 billion.

*Income policies.*—Even with continued budget restraint, the rate of inflation is unlikely to come down sharply as the economic recovery proceeds. Budget and monetary policies need to be supplemented with other approaches to wage and price moderation. As noted earlier, the voluntary pay and price standards, which the President introduced in 1978, played an important role in moderating wage and price increases during a highly inflationary period. After several years of good service, however, it is questionable whether these standards could remain effective if simply extended indefinitely in their current form. The administration will, therefore, be consulting during the remainder of this year with business, labor, and other groups to explore ways of achieving moderation in wage and price increases in 1981 and subsequent years.

## CONCLUSION

The administration's economic program for the 1980's is both responsible and dynamic. It builds on previous gains and addresses current problems. It establishes the basis for long-term growth that will both create permanent jobs and help contain inflation. At the same time, the administration's program provides assistance for workers and communities facing serious transitional problems.

The effects of this program will begin to be realized in a relatively short time. About 500,000 jobs will be created by the end of 1981 and a total of 1 million jobs by the end of 1982, in addition to those generated through normal economic recovery. And over the decade millions of jobs will be available to carry out the task of building our Nation's industrial might.

The administration intends to seek legislative action on this program early next year. The proposed policies will help shape our Nation's economic progress for many years and deserve careful consideration by Congress. It would not be desirable to attempt to hurry legislative action in the short time remaining before the national election.

While the economic measures respond to some of our most pressing economic challenges, they are not intended as the final answer or to be all-inclusive. Economic policy must continue to meet new circumstances and deal with new issues.

## Banking and Related Matters

### **Exhibit 30.—Remarks by Under Secretary Anderson, November 1, 1979, Before the 10th annual Intermountain Banking Seminar, Utah State University, Logan, Utah, on the challenges of competition and deregulation facing bankers and regulators**

I am delighted to be here with you and to be part of your 10th annual Intermountain Banking Seminar. While this is my first trip to Logan, Utah, your warmth and hospitality have made it a visit I will long remember.

I should also like to commend Assistant Dean Buehler and the many others who have been responsible for organizing this program. Over the years these seminars have become an important national forum for the discussion of financial issues.

Today's program is an excellent example of why these seminars come to represent such an important occasion for thought and dialogue. The issues that we discuss today touch each of us directly, as public officials, bankers, or consumers. But at the same time these issues transcend our individual interests, as they go to the very core of the economic well-being of our Nation. We have long since recognized that banking, and the depository sector generally, is one of the pillars of our economic society, the health and efficiency of which we disregard only at great peril.

Perhaps you will permit me a moment of historical reflection. A few days ago we noted the 50th anniversary of the event that has come to be known to history as the Great Crash. The marking of that melancholy affair produced a flurry of newspaper stories and reminiscences which have reminded us in vivid detail of that national trauma. While we are not immune to economic cycles and downturns even today, these stories should also serve to remind us how far we have come since the days of October 1929. Nowhere is this more evident than in the banking industry. Our predecessors in the public and private sector learned well the lessons of those days. They turned their cooperative efforts toward strengthening and revitalizing the banking sector. To the end that today we enjoy a banking system that is a model for other nations around the world. It is a system that is at once sound and robust, serving the needs of depositors and borrowers alike.

The very strength of the system that has been forged over the past 50 years should assist us in addressing the kinds of challenges that contemporary institutions must face. In this respect banking is no exception. Foremost among the challenges confronting bankers and regulators today are those of competition and deregulation. I mention these two challenges in the same breath because they are so closely related. We would misperceive in a fundamental way the nature of either of these challenges if we were to fail to recognize the necessary relationship of one to the other.

There is no better example of the relationship of these two concerns than in the current debate over Regulation Q and deposit interest rate controls. That debate provides a classic casebook demonstration of the dynamics of the regulatory and deregulatory process. But as many of you can attest, it is much more than an academic specimen. The future of the whole depository sector may well be determined by the outcome of that debate.

This administration has placed a special emphasis on the need to evaluate regulatory systems—with a keen awareness for the costs and benefits flowing from such systems. Consistent with this approach, the President established 2 years ago an interagency task force to review deposit interest rate ceilings and housing credit. Based on the work of that task force, the President in May of this year sent to the Congress a formal message on Regulation Q and financial reform.

The President's program for financial reform consisted of four elements. First, the President recommended that federally imposed interest rate ceilings on deposits at commercial banks and thrift institutions be gradually phased out. Second, the President recommended that federally insured commercial banks and thrift institutions be authorized to offer NOW accounts nationwide. To pay for higher cost deposits, the President also recommended that federally chartered thrift institutions be authorized to offer variable rate mortgages, and further that federally chartered thrift institutions be authorized to invest up to 10 percent of their total assets in consumer loans. This is a balanced program which addresses the needs of the small saver while at the same time providing additional earning powers to thrift institutions.

The President's recommendations were not new—earlier studies and commissions have come to the same general recommendations—but they were offered by the President with a new sense of urgency. Market developments had made it abundantly clear to the task force members that Regulation Q was simply not accomplishing its intended objectives of protecting depository institutions and the flow of mortgage credit. Instead, Regulation Q was serving only to perpetuate a rank injustice on the small saver.

We in the administration were convinced that prompt action by Congress was necessary to address these problems. Shortly after the President's message, the Senate Banking Committee developed legislation that embodied the President's major recommendations. That legislation has now become the centerpiece of a major financial reform effort.

At the core of that legislation is a provision that will phase out deposit interest rate controls and will move depository institutions toward free competition for funds. More precisely, the provision directs the regulators to increase the interest rate ceilings by at least one-half of 1 percent each year beginning in January 1982. However, any such increase could be postponed or reduced if the Federal Reserve Board, in consultation with the other regulators, were to determine that economic conditions or the economic viability of depository institutions so warrants.

The administration believes that it is absolutely essential that the Congress act this year to phase out interest rate ceilings along the lines proposed in the Senate legislation. Two concerns drive us to this conclusion.

The first is a simple concern for equity for the small saver. The current system is manifestly unfair to the small depositor. Large depositors receive market rates because of the exemption from the ceilings for CD's of \$100,000 or more. Those with at least \$10,000 can buy money market certificates and Treasury bills. But the small depositor who needs the liquidity of a passbook savings account is stuck with the 5¼ percent ceiling at commercial banks and the 5½ percent ceiling at thrift institutions. Of course, the greater liquidity of a passbook may require some sacrifice in yield, but the current disparity between short-term market rates and the passbook ceiling is simply too great an injustice.

Consider, for example, the case of an individual with a 5¼ percent passbook account at a commercial bank. If that individual is in a 30-percent marginal Federal income tax bracket, he or she would receive an after-tax yield of about 3¾ percent; and, of course, when further adjusted for inflation, the return is negative.

In effect, our depository regulations discourage savings. This prevents the small savers from improving their standard of living and security. On the larger level, it hurts our national economic performance by reducing the amount of our capital resources available for investment and productivity gains. In all of this you can see the outlines of a vicious inflationary circle. The combination of a high inflation and an artificially low deposit interest rate ceiling means that an individual is less likely to save and, if anything, more likely to consume. Reduced savings and increased consumption in turn mean more inflation. For the good of the individual saver as well as the overall economy, we must break that circle.

Second, in a very direct sense the health of our depository sector will depend on the phase-out of Regulation Q. We are witnessing today the signs of a fundamental shift in our financial markets. In past business cycles, rising interest rates have prompted an exodus of deposits, particularly from our thrift institutions. Investors and savers turned to alternative instruments and investments with returns above those prescribed for depository institutions. This disintermediation typically led to reduced earnings and capital generation at thrift institutions in particular and a sharp fall-off in mortgage lending.

In the current business cycle, the prospect of massive disintermediation has been deflected; or perhaps more accurately postponed, by regulatory initiative. As you know, last year the regulators authorized depository institutions to offer 6-month money market certificates with interest rates tied to market rates. This represented a fundamental step away from the philosophy of regulated ceilings. As it turns out, it may have been the only measure which has prevented a massive disintermediation from thrifts and commercial banks alike.



The deposit figures tell part of the story. In a little over a year the money market certificates have come to represent some \$200 billion worth of deposits in depository institutions. Over the same period of time, passbook accounts at commercial banks have grown little, if at all, while at savings banks and savings and loans passbook accounts have actually declined. The money market certificate has provided the only growth element in the depository sector. I think it is fair to conclude that without it the picture for depository institutions today would be bleak indeed. In one of those ironic twists that have increasingly come to characterize regulatory behavior, we were able to save Regulation Q—only by departing from it.

But the time for temporary expedients is fast coming to an end. Even the growth in the money market certificates cannot conceal the fundamental fact that depository institutions are losing, at a rapidly accelerating rate, their claim over the depository sector. As you know, there has been a veritable explosion in growth of nondepository intermediaries. The greatest challenge to date has come from the money market funds. Recent figures show that these funds now stand at some \$37 billion, up from approximately \$10 billion at the beginning of this year. Anecdotal evidence of their growth provides an additional perspective that the hard figures alone may not afford. I am told, for example, that because of the flood of new customers in recent weeks some of the funds have actually stopped accepting new customers until they can catch up with the backlog. I wish I could say that our depository institutions were blessed by the same problem. They are not.

All the evidence suggests that the money market funds will continue to expand at an ever increasing rate. I fear that we are witnessing the creation of a class of savers who have permanently moved outside the traditional depository sector. As a public policy-maker, I regard this as a dilemma. On the one hand, the growth of these funds attests to the fact that an ever increasing number of savers are unwilling to accept the constraints of rate, minimum denomination, and withdrawal penalty that characterize our depository accounts. The small saver, understandably, is looking for his break wherever he can find it. Equity as well as economics argue strong in his favor. On the other hand, the hemorrhage of funds from banks and thrifts may well undermine the traditional intermediary role of our depository institutions. This is a role that public policy has carefully promoted for decades. Now it seems that it is being abandoned or lost almost inadvertently.

These are stark words, but I am afraid that the situation merits, indeed requires, them. We have all become sensitive to the costs that unnecessary and inefficient regulation have imposed upon our society. There is a broad consensus developing in this Nation that we must do everything within our power to eliminate or reduce such unnecessary and inefficient regulation. But every great effort must have its beginnings and surely the revision of deposit interest rate ceilings must have its place in the forefront of our deregulation efforts. This deregulation will redound to the benefit of our Nation's savers and our Nation's depository institutions.

**Exhibit 31.—Remarks by Under Secretary Anderson, February 26, 1980, at the BGFO 1980 Direct Deposit Conference, regarding the direct deposit/EFT program**

It is an honor to be asked to participate in your direct deposit conference. The concept of direct deposit/EFT is one which has revolutionized our way of doing business, and it requires the understanding and cooperation of all of us in Government and in the private sector.

As a former banker in Georgia, I have followed with great interest in Treasury the progress of the Government's efforts to improve and enhance the direct deposit program. As most of you probably know, the very first EFT payments by the Government were made in Georgia in February of 1976. Since that time, the cumulative volume of EFT payments has exceeded 300 million. Of course, it is no surprise to me that Georgia was willing to be the first to be so forward-looking! I am also proud of the significant contributions which the Federal banks of Atlanta made in the beginning of the program.

Great strides have been made since the first direct deposits of checks were made in September 1975. There is still much to be done, however, and I would like to discuss briefly where we have been and where we plan to go with this program.

By the end of calendar year 1976, there were approximately 5.1 million participants in the direct deposit program. In 1977, the program was expanded to encompass all types of Federal recurring benefit payments. As of December 1979, enrollment in the program had increased to 11.2 million, over a 100-percent increase in 3 years. This increase is in large measure due to the excellent job done by both the private sector and the staff of the Bureau of Government Financial Operations in bringing the advantages to the attention of the public and business.

The program has received some justified high visibility and publicity. In the Bank Systems and Equipment readers poll, which selected the decade's top 10 people and events that shook the bank operations scene, the direct deposit of social security checks was selected as the number two event. In the individual category, Mr. Lester W. Plumly, Assistant Fiscal Assistant Secretary for Planning and Research, was selected as the number three individual for his involvement in putting together the program. We at Treasury are very proud of these accomplishments.

In addition, the Office of Personnel Management, in a recent management conference, highlighted Treasury's direct deposit program as a fine example of increased productivity and improved service to the public. In this administration, with its strong emphasis on cutting the Federal expenditures, the savings of \$17 million in 1979, with projected savings by 1981 of \$30 million plus, are extremely important.

I understand that NBC, which is doing a documentary on improved productivity in Government, has also focused on the direct deposit program.

Although 26 percent of those receiving recurring Federal benefit payments are now participating in the direct deposit/ EFT program, there is much left to be done. I know that the remainder of the program today will focus intensely upon what plans you all have to continue the successful start of the program and to build upon the wonderful foundation already in place.

Treasury is making a concerted effort to convert all classes of payments to electronic funds transfer. These include additional classes of military payments as well as Federal tax refunds, VA insurance and public debt interest and vendor payments. Treasury's goals are to have 55 percent of all eligible payments included in the program by 1985 and 80 percent by 1990. In order to achieve these goals, Treasury is continuing to work with Federal agencies, the Federal Reserve, the financial community and the payment recipients.

The program is not without some problems with regard to public acceptance. Believe me, after my recent experiences with the new \$1 coin, I can safely say that I know that people are resistant to change until you have convinced them beyond a doubt that the change holds great advantages for them. I certainly believe that a reasonable observer would have to acknowledge that the direct deposit program offers great advantages to the public and private sectors.

All of you are familiar by now with the cost benefits to be realized by increased participation in the program. In issuance costs alone, there can be a savings of 3 cents by use of EFT rather than use of a check. Figured in the cost of a check are personal services and benefits, including overhead; supplies and materials; equipment, both purchased and rented; and space and utilities involved in check disbursement operations, check payment and reconciliation operations, and check claim operations.

In addition to these costs there are also postage costs to be considered. The bottom line of direct deposit is that Treasury is deriving a net 70-percent savings over the check system, which far offsets any concern about the cost of float or the EFT system itself. These black and white figures do not, of course, give a value to the major improvements in both the system and the level of service.

The customer derives a good bit in savings in time and aggravation. The safety of the system eliminates the possibility of lost, stolen, or delayed checks. Even while traveling or away from home, the funds will be available on a certain date. The aggravation of waiting in crowded lobbies and long lines is eliminated. The whole idea of service is exemplified in the direct deposit program. The national blood pressure level should be considerably lower already.

For the financial organizations in the country there can be distinct advantages as well. The cost of payment processing is reduced and there is an increase in the efficiency of payment processing. More time is left for individualized banking assistance to customers. Forged Government checks become less of a problem. There are, no doubt, other advantages which each of you could add to the list.

We are at a crucial point in the program. In the next 5 years we want to more than double the percentage of participants. That is going to take a lot of additional hard work on the part of all of us. Without the help of the private sector, Treasury would have been at a loss to get the program off the ground, and will be unable to meet its goal.

I hope that you are here to dedicate yourselves and your institutions to carrying on the good work already begun. I know that Treasury is committed to making the program, which is a high priority, even more successful.

In reviewing what our next steps will be, I hope that we will keep in mind the impact of the changes upon financial institutions that full implementation of the program may have. There should be careful planning to assure that the next phase of the direct deposit/EFT program is worked out in conjunction with the concerned entities, just as the initial phases were developed. If we don't have the full support at each step along the way of the agencies and private sector, we will undermine our good beginning.

Thank you for the opportunity to meet with you this morning. The work you are doing is exciting and innovative. It is a good example of Government and business working hand-in-hand to serve the public. Each of us benefits from your efforts.

**Exhibit 32.—Remarks by Under Secretary Anderson, September 23, 1980, at the 10th Annual International Fellows Conference, Johns Hopkins University, Baltimore, Md., on cooperation and communication between Government and business**

It is a privilege to welcome you to this session and to be on the platform with a distinguished group of people who are involved on a daily basis with almost every issue of importance at this conference. As a banker for 27 years, I have been very sensitive, during my 4 years in the Treasury Department, to the frustrations that the private sector often feels when Government gets involved in what has been traditionally done by the business community. I believe that our panelists today can give us insight into how we might work to improve the cooperation and communication between Government and business and work toward productive growth and progress in our urban centers.

While all of us would like to think, perhaps, that everybody would be a whole lot better off if Government would just disappear, each of us has our favorite regulation or favorite program or favorite cause which Government protects or promulgates. It is time for the pendulum to center itself in some respects. Our purpose here today is to delve into the ways in which the private sector and Government can join together in the last two decades of this century to avoid wild swings which bring about over-regulation or neglect. I believe the process has already well begun.

The importance of the subject which has brought us together today is hardly a matter of dispute. The changes which have occurred over the last 20 years have made the economic challenges of the 1980's substantially different from those we faced in 1960 and in 1970. We have seen tremendous growth in the importance of international trade to the U.S. economy along with a quantum leap in the competitiveness of many foreign economies. We have also faced a tremendous surge in the growth of the labor force—a surge which we have absorbed with remarkable success though certainly not without a cost in terms of productivity gains. We have learned to place greater emphasis on social priorities such as cleaner air, cleaner water, and safer, healthier work environments. Influencing these developments—and influenced by them—the pace of technological change has also accelerated.

While the results of many of these developments have been favorable, there have also been some unfavorable effects. In some cases industrial dislocation has left workers without jobs, and towns and cities with a loss of part of their income base.



Future reindustrialization, or whatever we choose to call it, will create similar disruptions that will present us with a significant challenge.

The 1980's will not be a successful decade if we insist upon meeting these new challenges with ideas that were appropriate 10 or 20 years ago. Revitalizing American industry will require a new spirit of cooperation among business, labor, and government.

Unquestionably, the great strength of the American economy has been in its primary reliance upon the private enterprise system, and that fundamental proposition will continue to be true. But the character of American industry and the skills it needs are in fact changing, and there is no denying actions of government at the Federal, State, and local levels increasingly affect our industries. Government has, and continues to bear, responsibility for creating a climate which encourages private investment and the creation of permanent, productive private-sector jobs. In our present circumstances, however, government and the financial sector must work together even more extensively if they are to smooth the adjustment process.

In his economic program announced August 28, the President included a number of proposals which should help engender this cooperation and expedite the adjustment process. Foremost among these is a proposal directly aimed at encouraging the cooperative efforts of Government and the private sector. The President proposes to establish an Economic Revitalization Board comprised of representatives from industry, labor, and the public to advise the President on the many complex issues which we face in revitalizing our economy. The board will also develop specific recommendations for establishing an Industrial Development Authority to provide financial assistance for industrial and economic revitalization in areas hard hit by the recent economic changes. It is expected that the Industrial Development Authority will mobilize both public and private resources, including capital from private markets and pension funds.

The President's program also addresses the problem of encouraging private capital investment. To achieve this end, several tax changes will be proposed. A new system of liberalized depreciation allowances is expected to encourage businesses to expand investment, to modernize productive capacity, and to provide new jobs. To assist businesses suffering from temporary losses or reduced profits which blunt the incentive effects of the investment tax credit, the administration will propose that 30 percent of earned but unused investment tax credits be made refundable beginning in 1981. There is also a proposal to reduce labor costs and further encourage employment by providing a 2-year social security tax credit designed to offset the social security tax increase for employers. This is scheduled to take effect in 1981. Small business will, of course, benefit from these tax proposals, but, in addition, the administration will also recommend liberalizing Subchapter S requirements to enable more investors to participate in new ventures, thus providing easier access to capital.

Regulatory reform is another aspect of the movement toward greater Government/business cooperation. Regulatory costs influence investment because of the outlay required to achieve compliance and because of the impact on the cost of new plants per unit of output. While we must continue to recognize health, safety, and a clean environment as being important national goals, we must also recognize reform as an important element in policies to promote a healthy economic environment.

Export promotion represents an area of renewed business/Government cooperation. To accomplish this renaissance, we have increased support to the Export-Import Bank more than sevenfold over the last 4 years, and the Government programs which support U.S. international trade have been reorganized and combined to make them more effective. The administration will also propose an amendment to the Internal Revenue Code to provide for an exclusion for income earned abroad in certain areas.

The President's program provides special encouragement for private investment and public development capital in areas in transition. Basically, this comes down to substantially increased Government support for economic development. The administration proposes to increase the Economic Development Administration's program level from the \$600 million in fiscal year 1980 to \$1.7 billion in fiscal year 1981. To enhance public efforts, it is proposed to increase program levels by \$1 billion for fiscal year 1981 and \$2 billion for fiscal year 1982 for economic and industrial development programs. Finally, the administration will propose a special targeted investment tax

credit of 10 percent for eligible investment projects in localities of particularly high unemployment.

It is also clear that Government has a role to play in assuring the development of the economic infrastructure necessary for the private sector to operate efficiently. Generally, this translates into tending to the need for an efficient transportation system. To this end, the Congress has before it a program for restructuring the Nation's railroad system, mass transit facilities, airports and airways, and the 1981 budget contains \$8.4 billion to complete and repair the Federal highway system.

Some of the forms of public/private cooperation I have cited may not be all that new. But the general realization and the desire that such cooperative relationships between Government and the private financial sector must and can be made to work effectively is relatively new. To explore the ways in which Government and the private sector can work together more successfully in the financial sector is what brings us here this morning.

### Mint Operations

#### Exhibit 33.—An act authorizing the President of the United States to present a gold medal to the American Red Cross

[Public Law 96-138, H.R. 4259, December 12, 1979]

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That (a) the President is authorized to present, in the name of Congress, an appropriate gold medal to the American Red Cross, in recognition of its unselfish and humanitarian service to the people of the United States. For such purposes, the Secretary of the Treasury shall cause to be struck a gold medal with suitable emblems, devices, and inscriptions to be determined by the Secretary. There are authorized to be appropriated not to exceed \$15,000 after October 1, 1980, to carry out the purposes of this subsection.

American Red Cross. Gold medal.

Appropriation authorization.

(b) The Secretary of the Treasury may cause duplicates in bronze of such medal to be coined and sold under such regulations as he may prescribe, at a price sufficient to cover the cost thereof, including labor, materials, dies, use of machinery, overhead expenses, and the gold medal, and the appropriation used for carrying out the provisions of this Act shall be reimbursed out of the proceeds of such sale.

Duplicates.

(c) The medals provided for in this Act are national medals for the purpose of section 3551 of the Revised Statutes (31 U.S.C. 368).

#### Exhibit 34.—An act to authorize the President of the United States to present on behalf of the Congress a specially struck gold medal to Ambassador Kenneth Taylor

[Public Law 96-201, H.R. 6374, March 6, 1980]

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That (a) the President of the United States is authorized to present, on behalf of the Congress, to Ambassador Kenneth Taylor, a gold medal of appropriate design in recognition of his valiant efforts to secure the safe return of six American Embassy officials in Tehran. For such purpose, the Secretary of the Treasury is authorized and directed to cause to be struck a gold medal with suitable emblems, devices, and inscriptions, to be determined by the Secretary of the Treasury.

Ambassador Kenneth Taylor. Commemorative medal.

There are authorized to be spent from already appropriated funds not to exceed \$20,000 to carry out the provisions of this subsection.

Cost.

Duplicates.

(b) The Secretary of the Treasury may cause duplicates in bronze of such medal to be coined and sold under such regulations as he may prescribe, at a price sufficient to cover the cost thereof, including labor, materials, dies, use of machinery, overhead expenses, and the gold medal, and the appropriation used for carrying out the provisions of this subsection shall be reimbursed out of the proceeds of such sale.

31 U.S.C. 368.

(c) The medals provided for in this Act are national medals for the purpose of section 3551 of the Revised Statutes (31 U.S.C. 368).

**Exhibit 35.—Titles II, V, and VI of an act to provide for the transfer of the Foreign Claims Settlement Commission of the United States to the United States Department of Justice as a separate agency; \* \* \* and for other purposes (abolition of the Annual Assay Commission)**

[Public Law 96-209, H.R. 4337, March 14, 1980]

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the purposes of this Act are as follows:*

## TITLE II—ANNUAL ASSAY COMMISSION

Abolition. 31

U.S.C. 363 note.

Transfer of functions.

The Annual Assay Commission, and the positions of Assay Commissioners established by section 3547 of the Revised Statutes of the United States (31 U.S.C. 363), as amended, are hereby abolished. The functions of that Commission and of the Assay Commissioners are hereby transferred to the Secretary of the Treasury.

## TITLE V—DETERMINATION ORDER

22 U.S.C. 1622a

note.

The Director of the Office of Management and Budget is authorized and directed to make such determinations as may be necessary with regard to the transfer of functions, powers, and duties pursuant to this Act, and to make such additional incidental dispositions of personnel, assets, liabilities, property, records, and unexpended balances of appropriations, authorizations, allocations, and other funds held, used, arising from, available to or to be made available in connection with the functions transferred by this Act, as the director may deem necessary to accomplish the purposes of this Act. The Director is further authorized and directed to provide for terminating the affairs of each agency, board, or commission abolished by this Act.

## TITLE VI

Effective date. 22

U.S.C. 1622a note.

This Act shall take effect on the date of enactment.



**Exhibit 36.—An act to authorize the President of the United States to present on behalf of the Congress a specially struck gold medal to Simon Wiesenthal**

[Public Law 96-211, S. 1792, March 17, 1980]

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That (a) the President of the United States is authorized to present, on behalf of the Congress, to Simon Wiesenthal, a gold medal of appropriate design in recognition of his contribution to international justice through the documentation and location of war criminals from World War II. For such purpose, the Secretary of the Treasury is authorized and directed to cause to be struck a gold medal with suitable emblems, devices, and inscriptions to be determined by the Secretary of the Treasury. There is authorized to be appropriated not to exceed \$15,000 after October 1, 1980, to carry out the provisions of this subsection.

Simon Wiesenthal.  
Commemorative  
medal.

(b) The Secretary of the Treasury may cause duplicates in bronze of such medal to be coined and sold under such regulations as he may prescribe, at a price sufficient to cover the cost thereof, including labor, materials, dies, use of machinery, overhead expenses, and the gold medal. The appropriation made to carry out the provisions of subsection (a) shall be reimbursed out of the proceeds of such sales.

Appropriation au-  
thorization

Duplicates.

(c) The medals provided for in this Act are national medals for the purpose of section 3551 of the Revised Statutes (31 U.S.C. 368).

## Enforcement and Operations

**Exhibit 37.—Address of Assistant Secretary Davis, October 9, 1979, before the Federal Interagency Polygraph Seminar, FBI Academy, Quantico, Va., on the use of polygraph examinations in criminal investigations and in employment screening**

It is a pleasure to join you today and to have this opportunity to share my impressions of the place that polygraph examinations should occupy in Federal criminal investigations and employment screening for particularly sensitive positions.

As we are aware—sometimes painfully so—in the past few years both the law enforcement and intelligence communities have undergone far-reaching and intensive examinations of their authorities, principles, goals, and methods of operation. Techniques and purposes which once were presumptively appropriate (and in some cases even specifically mandated by Congress) have been dissected and challenged within the executive branch, before Congress, in the courts, and in the press and other public forums.

In the arena of criminal justice, those of us who have been criminal investigators and prosecutors have been accustomed to having the circumstances of the execution of basic criminal investigative procedures and police powers challenged routinely by counsel for the criminally accused. This is expected in the course of achieving constitutionally mandated due process even if at times those of us in the enforcement community may feel that the criminal suspect or defendant has all the high cards. Of course, the give and take of our criminal justice system has dealt directly with the use

of polygraph examinations and continues to do so since the admissibility of the results of polygraph examinations is not a settled matter of law.

The new phenomenon—the one which we are experiencing along with the intelligence community—is the questioning of principles and procedures, and the philosophies and goals intertwined with them, from which the authority and justification of many of our activities arise. Far more than simply the propriety of how a mission was executed is at stake in these controversies. Both constitutional principles and the basic goals of our society are under scrutiny in multiple arenas, and the balancing of national purpose, constitutional requirements, and the missions of our many enforcement and intelligence agencies produce diverse alternative futures for our agencies and our means of accomplishing their missions.

For the law enforcement agencies the arena of controversy is not expanded as greatly as are the participants. To the routine characters of courtroom and congressional committee are added a new class of policy advocates and group litigants who use coordinated campaigns in the courts, in Congress, in the press and in the councils of the executive branch to seek changes that may fundamentally alter the criminal investigative process.

I think it is fair to say that the intelligence community has experienced a considerably greater shock from this phenomenon. Methods and technologies that a few years ago were known only to a select few whose tasks required it, have now been examined by committees of Congress in open as well as closed sessions. Activities and operations which governments normally would take extreme measures to disavow regardless of their actual responsibility have been displayed before the world in excruciating detail. A deluge of books, articles, news stories, and interviews have accompanied this new "official" openness, and it has been crowned by the growth of litigation directed at activities, records, and techniques of our intelligence agencies. Indeed, this impressive escalation of legal actions involving intelligence agencies and such issues as "gray-mail" has established a new legal specialty of "intelligence law."

How does this experience relate to the utilization of polygraph techniques by Federal agencies? I believe it is clear from the recurring congressional interest in polygraphs as well as the broad expanse of other law enforcement and intelligence techniques that all procedures which have even an aura of intrusiveness into perceived privacy interests are going to remain subject to some form of systematic and external scrutiny. In the case of our intelligence agencies it seems well established that the House and Senate Select Committees on Intelligence are not transient investigating bodies but are genuinely permanent oversight entities. With or without the adoption of some form of "charters legislation" for the intelligence community, these committees will be involved deeply in issues of the legality, propriety, and wisdom of intelligence collection objectives and techniques.

The Federal criminal investigative agencies clearly will be receiving similar attention from committees such as the House and Senate Judiciary Committees. Furthermore, this congressional attention has already been joined by executive initiatives—in particular the FBI Charter legislative proposal that the President transmitted to Congress at the end of July. Similarly, in the intelligence community two Presidents have promulgated Executive orders which impose responsibilities and limitations upon those agencies engaging in foreign intelligence activities; and, thus, the executive branch has instituted its own internal standards and controls in these sensitive and controversial areas.

Both the criminal investigative and intelligence communities are sharing in the internal and external attention to issues which are notable for their commonality. In either context, issues of the means, extent, and intensity of information collection activities, as well as the uses and exchange of that information, are central to both individual agency and executive branch procedures and to the various legislative proposals which have appeared in Congress. In addition to safeguarding privacy interests through Executive mandates and possible legislation, we find that our shared concerns for the security of confidential sources and the sensitive information collected through them and for clear authority to acquire important data are also addressed through agency procedures and legislative initiatives.

The use of polygraph examinations in criminal investigations and in employment screening clearly raises closely related issues of protected privacy interests and the

competing need of agencies to acquire information and to measure its veracity and reliability. Obviously, during the considerable attention directed at other investigative and intelligence procedures, the utilization of polygraphs has not been ignored and clearly has engendered, and continues to produce, controversy within both Congress and the executive branch. I understand that in an unclassified report to be issued momentarily by the House Permanent Select Committee on Intelligence those executive branch agencies involving numerous employees in critical-sensitive positions are criticized for the disparity in their methods of preemployment background investigations. It appears that one of the issues which the report discusses is that of employment screening with polygraph examinations and that the Select Committee will recommend that the Director of Central Intelligence oversee some form of interagency study on the value of the polygraph in these circumstances. Now in such a case, it is clear that this congressional committee is seeking to balance the competing interests of having the best possible forms of preemployment and employee security investigations against using techniques of truth verification which may not have the reliability necessary to enhance security investigations and to outweigh the obvious intrusion into the privacy of the subject individuals. Clearly, one does not have to accept the premise that polygraph reliability is not adequately established in order to recognize that the issues raised by such a report are valid and that they fit into the greater milieu of privacy interests versus investigative and intelligence needs.

As polygraph examiners and the supervisors of such examiners you have, in my judgment, an opportunity and a responsibility for contributing to the balancing of these competing interests and for placing them in perspective with the various related issues challenging the Federal law enforcement and intelligence communities. Basic concepts of civil liberties unavoidably compete with equally basic concepts of governmental obligations to protect the Nation's security and to suppress crime. The strength of our dynamic constitutional system is that it should find the appropriate balance among such competing interests and maintain it without subjecting them to inflexibility or to vagueness. For the governmental process thus to operate, those most knowledgeable in the fields of contention must contribute actively to understanding and to the construction of standards and procedures which serve these sometimes contentious goals and principles.

The relationships developed and knowledge gained through the type of interagency cooperation demonstrated by this seminar should enhance the continuing examination of these issues and the establishment of the best means of managing them. I encourage you in those efforts and wish you every success.

**Exhibit 38.—Press release, October 29, 1979, guidelines for determining which Presidential candidates should be recommended for Secret Service protection**

The Advisory Committee for Presidential and Vice Presidential candidate protection today released a formal set of guidelines for determining the 'major' candidates who should be recommended to the Secretary of the Treasury for Secret Service protection.

A copy of the guidelines follows.

The Committee, which was established under Public Law 90-331, consists of five members:

Speaker Thomas P. O'Neill, Jr.  
House Minority Leader John Rhodes  
Senate Majority Leader Robert Byrd  
Senate Minority Leader Howard Baker  
Former Congressman Wilbur Mills

The fifth member, who is designated by the four congressional members, was selected by the Committee at its first meeting on October 24.



ADVISORY COMMITTEE GUIDELINES FOR ASSIGNMENT OF SECRET SERVICE  
PROTECTION TO PRESIDENTIAL CANDIDATES PURSUANT TO PUBLIC LAW 90-331  
(1980 PRESIDENTIAL CAMPAIGN)

I. Introduction

Public Law 90-331 places upon the Secretary of the Treasury (the Secretary) responsibility for determining, from time to time after consultation with an Advisory Committee (the 'Committee'), those persons who qualify as a major Presidential and Vice Presidential candidate (major candidate) and thus should be furnished with Secret Service protection, unless declined. The Committee consists of the Majority Leader of the Senate, the Minority Leader of the Senate, the Speaker of the House of Representatives, the Minority Leader of the House of Representatives, and one additional member to be selected by the members of such Committee. These guidelines will assist the Committee in advising and the Secretary in determining who are the 'major Presidential or Vice Presidential candidates who should receive . . . protection . . .'

II. Persons Defined as Major Candidates

A. Nominees for Offices of President and Vice President The nominees for the Office of President and Vice President of any party shall be deemed to be major candidates when the candidate for the Office of the President of that party in the preceding Presidential election received ten percent or more of the total number of popular votes received by all candidates for the Office of the President of the United States.

B. Candidates in Primary Elections Prior to the national conventions of the candidate's party, a candidate seeking the nomination for President of a party shall be deemed to be a major candidate when—

- (1) The candidate has publicly announced his or her candidacy;
- (2) The candidate is seriously interested in, and actively campaigning on a national basis for the office for which his or her candidacy has been announced; and
- (3) a. The candidate has (i) qualified for and remains qualified for matching payments under Sections 9031 through 9042 of Title 26, U.S. Code in an amount of at least \$100,000 for the Presidential campaign for which nomination is sought (whether or not the candidate declines matching funds) and (ii) has received additional contributions totaling \$900,000 or more in compliance with the Federal Election Campaign laws; or  
b. The candidate, in two consecutive primary elections, has received at least ten percent of the total number of votes cast for all candidates of the same party for the same office in such primary election.
- (4) The candidate is seeking the nomination of a party whose nominee is eligible for protection under IIA.

III. Commencement and Duration of Protection of Major Candidates

A. *Commencement of Protection.* No protection shall be furnished pursuant to P.L. 90-331 earlier than January 11, 1980. On or after such date, protection shall be commenced forthwith upon a determination by the Secretary that a person is a major candidate.

B. *Duration of Protection.* Protection shall not be withdrawn so long as a major candidate continues to qualify under the terms of Section II.

IV. General

Nothing contained herein shall preclude the Secretary, after consultation with the Committee, from providing protection to a major candidate although the requirements and conditions contained in parts II and/or III of these guidelines have not been met.

**Exhibit 39.—Statement of Assistant Secretary Davis, February 13, 1980, before the Subcommittee on Monopolies and Commercial Law of the House Committee on the Judiciary, in support of the Customs Courts Act of 1980**

I am pleased to have the opportunity to testify today in support of H.R. 6394, the Customs Courts Act of 1980. This Department supported S. 1654, a similar bill sponsored by Senator DeConcini, which was passed late last year by the Senate. We commend you and your staff, Mr. Chairman, for the efforts that have been devoted to this bill and fully support its enactment.

This bill would create a comprehensive system of judicial review of civil actions arising from import transactions and other statutes affecting international trade. It would clarify and expand the jurisdiction of the Customs Court and insure that the court has the remedial powers to redress injuries suffered by persons engaged in international trade.

We in the Treasury Department have long recognized that the United States Customs court was being underutilized while increased litigation having a significant impact on international trade was being instituted in the district courts. Moreover, in the last 2 years, there have been significant legislative initiatives in the area of international trade. Both the Trade Agreements Act of 1979 and the Customs Procedural Reform and Simplification Act of 1978 have expanded the rights of adversely affected parties to judicial review. Consequently, we anticipate that unless this bill is enacted, a significant increase in trade litigation will add to the enormous workload of already overburdened district courts.

To illustrate this point, a recent amendment to section 592 of the Tariff Act of 1930, the so-called fraud provision, authorizes a trial de novo in an action to collect a penalty assessed under that section with the burden placed on the Government to establish the degree of culpability of the violator. Prior to passage of this amendment, the structure of the law all but eliminated judicial review of these penalties. Now, we anticipate judicial review will be sought more frequently. Under existing law, the Government is required to institute such collection actions in the district courts. The bill under consideration today would require such actions to be commenced in the Court of International Trade. While it is difficult to estimate the number of court actions per year which will be filed as a result of new section 592, we believe the number will far exceed the approximately 200 cases filed in the district courts in FY 1979. In our view, judicial efficiency and economy require that the many technical issues which surround penalties arising out of false and fraudulent customs transactions be considered by a court versed in this somewhat esoteric area of the law.

We are concerned with one provision in H.R. 6394 which relates to the review of rulings or the refusal to issue or change a ruling regarding technical customs matters such as classification, valuation, entry requirements, and vessel repairs. New section 1581(j)(2) would give the Court of International Trade jurisdiction to review such rulings or the refusal to issue or change such rulings if a person demonstrates that he would be irreparably harmed by having to wait and file a protest against later Customs action based on the ruling.

The Customs Service issued over 13,800 rulings to members of the public in 1979. Under current law, judicial review of these rulings can be obtained by an importer only after an importation has occurred and pursuant to an administrative protest which is denied. Similarly, an American manufacturer, producer, or wholesaler of merchandise similar to the imported merchandise may only obtain review of rulings affecting his products pursuant to section 516 of the Tariff Act by filing a petition with the Customs Court challenging the ruling of the Customs Service when it is applied to an actual importation. In each instance, the Customs Service decision is reviewed by the Customs Court in a trial de novo.

We strongly believe that this current method of obtaining review ought to be maintained. The keystone under existing law is the existence of an actual importation. It is essential for the stability of the ruling process that the treatment of an actual importation be at issue, otherwise the court will be overburdened with hypothetical cases. Judicialization of the Customs informal ruling process will discourage it from providing useful guidance to the public. We also do not believe the Congress would want the new Court of International Trade to replace the administrative agency now

assigned the ruling responsibility. In addition, very few importers would import merchandise, protest, and pay the duties in order to challenge Customs Service treatment of certain merchandise if they could obtain judicial review without an actual importation and without the payment of duties.

However, if the Committee finds that there are circumstances in which the traditional method of obtaining judicial review of Customs Service rulings is too restrictive and that some modification is necessary, we strongly believe that any modification should be extremely limited and applicable only to those instances in which a modification is truly necessary.

In any event, there is no justification for extending this remedy to American manufacturers, producers, and wholesalers as this bill would do. Absent an importation which is adequately covered by section 516, any harm to an American manufacturer is speculative at best. In the Senate bill the opportunity to obtain judicial review prior to exhaustion of administrative remedies applied only to importers. As we have stated, we do not believe any changes are necessary. However, if the Committee believes otherwise, we recommend that the Senate provisions, with the modifications indicated below, be adopted. Section 516 has long provided an adequate remedy to American manufacturers, producers, and wholesalers. During the past several years both the House Ways and Means Committee, and the Senate Finance Committee considered amendments to section 516. Although 516 was expanded to include parties such as American labor unions which, traditionally, had been excluded from its coverage, we find it significant that these committees did not alter the basic statute or provide an opportunity to challenge a ruling or the refusal to issue or change a ruling before the importer actually brought the competitive product into the country.

Furthermore, it is likely that an opportunity to challenge rulings or the failure to issue or change rulings would become an unintended tactical weapon of American manufacturers and producers in their constant battle with importers for markets, risking the creation of undesirable trade barriers.

Finally, if there is to be a provision for declaratory review of occasional rulings, it should be narrowly confined to those persons who demonstrate actual need. As now drafted, the bill appears to allow much broader use because of the general language of section 2631(f) on standing, section 2636(g) on time limits for suits, and the absence of any requirement that the Customs Service be given adequate time to respond to a request for a ruling.

I have attached as part of my statement technical comments and suggestions which I hope this committee will consider.

## TECHNICAL COMMENTS

### TITLE II

#### Section 1581(a)(4)

The court of International Trade would be granted exclusive jurisdiction over a civil action where the administrative decision involves the exclusion of merchandise from entry or delivery or a demand for redelivery to Customs custody (including a notice of constructive seizure) under any provision of the customs laws.

The parenthetical phrase 'including a notice of constructive seizure' is not appropriate. Seizure, whether actual or constructive, does not occur when merchandise is excluded or there has been a demand for redelivery. Seizure occurs where the law provides for seizure subject to forfeiture, and where a statute authorizes seizure to secure payment of a penalty.

The Court of International Trade has not, other than in this section, been given jurisdiction over actions involving seizures and forfeitures. The parenthetical phrase should be deleted.



**Section 1581(j)(2)**

As noted, we prefer no provision granting an exception to the traditional method of obtaining judicial review, but if an exception is included we prefer a provision similar to that contained in S. 1654. The paragraph should be amended to read:

The Court of International Trade shall not have jurisdiction— . . .

(2) to review any ruling or refusal to issue or change a ruling relating to classification, valuation, rate of duty, marking, restricted merchandise, entry requirements, drawbacks, vessel repairs, and similar matters issued by the Secretary of the Treasury other than in connection with a civil action commenced under subsection (a) of this section, except that this exclusion shall not apply if a person, after exhausting such procedures as the Secretary of the Treasury may by rule provide, demonstrates that, without a substantial doubt, it would be commercially impractical to obtain judicial review under subsection (a), and the person would otherwise suffer substantial irreparable injury. If the person fulfills the conditions set forth in the preceding sentence and demonstrates that the Secretary's ruling or refusal to change a ruling is arbitrary or capricious or otherwise contrary to law, the Court shall award appropriate relief.

**Section 1582(b)**

In paragraph (1), subsection (a) should be corrected to read subsection (a)(1).

Since a section 592 case may involve entries in several districts, subsections 1582(b)(1) and (b)(2) should be changed to indicate 'an appropriate district court'. Subsection 1582(b)(2) currently contains no provision to prevent forum shopping by requesting a jury trial, obtaining a transfer of the case to a district court, and then withdrawing the request. A new sentence should be added at the end of the subsection as follows: 'If the jury trial motion is later withdrawn or denied, the case shall be remanded to the Court of International Trade for further proceedings.'

**Section 1583**

This provision grants the Court of International Trade exclusive jurisdiction to render judgment upon any counterclaim of the United States to recover customs duties relating to such transaction. Inasmuch as most actions against the United States to recover customs duties arise under section 514 and payment of "customs duties relating to such transactions" are a jurisdictional prerequisite, that phrase would have little, if any, effect. In our opinion, the Court should be given exclusive jurisdiction over any counterclaim of the United States to recover any duties or penalties arising out of an import transaction which are owed by the importer to the Government. This would avoid numerous actions by the Government against the same importer in the Court of International Trade to recover unpaid customs duties pursuant to section 1583(a)(1) and (3).

**Section 1584**

In both subsection (a) and subsection (b) the word "shall", the first time it is used in each subsection, should be changed to "may" in order to give the district courts discretion to dismiss a case where institution of the action in that court was for purposes of evading the rules of the Court of International Trade or for any other improper reason.

**TITLE III****Section 2637(a)**

The provision relating to exhaustion of administrative remedies should include a cross-reference to section 1581(j)(2) which, in effect, permits Court review prior to exhaustion of the administrative remedies provided in the Tariff Act. The provision should also address the disposition of monies found by the Court of International

Trade to have been unjustly collected by the Government where the action resulting in the finding was not brought by the importer. This could occur where the importer's surety commenced the civil action. Under the law the surety may recover only the amount of the liquidated duties, charges or other exactions that he paid on the entries. The balance of the monies should remain in the Treasury of the United States.

#### **Section 2643(c)(1)**

This provision would permit the Court of International Trade to issue a preliminary or permanent injunction upon the motion of a person who would have the right to commence a civil action after exhausting all appropriate administrative remedies. The Court is directed to consider whether the person making the request will be irreparably harmed if such injunction is not granted and the effect of granting such injunction on the public interest. The relationship between this provision, section 2637 and section 1581(j)(2) is not clear. We prefer the similar provision, section 2643(a), contained in S. 1654, which permits the Court to order an appropriate form of relief, including injunctive, but apparently within the confines of the jurisdictional sections and the provision relating to exhaustion of administrative remedies.

#### **Section 2646(1) and (3)**

In establishing the precedence to be given cases in the Court of International Trade, the exclusion of perishable merchandise contained in (1) should be expanded to include the redelivery of such merchandise. With regard to (3), the words "commenced under section 515 of the Tariff Act of 1930" are unnecessary and should be deleted.

### **TITLE IV**

#### **Section 2602**

The comments relating to section 2646 are applicable to this section.

#### **Section 1546(1)**

It is inappropriate to place review of the denial of a customs broker's license under section 641(a) of the Tariff Act of 1930 in the Court of Appeals for International Trade, Patents, and Trademarks, because there is no statutory requirement that the Secretary construct a formal record to support such actions. Review of such denials should be left to a trial court where such a record may be constructed. It would be a substantial and unwarranted burden to require the Secretary to construct such a record in view of the small number of cases in which a denial is actually contested.

#### **Exhibit 40.—Statement of Assistant Secretary Davis, May 8, 1980, before the House Subcommittees on International Economic Policy and Trade, and Europe and the Middle East, of the House Committee on Foreign Affairs, on actions taken by the administration to deal with events in Iran**

I appreciate the opportunity to appear before you to discuss actions taken by the administration pursuant to the International Emergency Economic Powers Act (IEEPA) in order to deal with the continuing threat to the national security, foreign policy, and economy of the United States created by events in Iran.

These events have served to emphasize the desirability of the kinds of emergency powers which IEEPA places at the President's disposal. On this first occasion of the use of IEEPA, the Subcommittee on International Economic Policy and Trade can derive satisfaction from the fact that IEEPA, in whose creation the Subcommittee was so instrumental, has proved to be workable and effective.

American hostages were taken in Tehran on November 4, 1979. Then, news reached the United States that the Iranians were planning further actions directed at U.S. financial institutions, actions which also threatened harm to the international financial system. There can be little doubt that these actions created, in the language of IEEPA,

an "unusual and extraordinary threat" to the national security, foreign policy, and economy of the United States.

In response to this threat, after consultations between administration officials and the congressional leadership, the President signed an Executive order at 8:10 a.m. on November 14, 1979, blocking transfers of property or interests in property of the Government of Iran, its instrumentalities and controlled entities, and the Central Bank of Iran. This action by its terms did not apply to the property of private Iranians. It also did not transfer title in the blocked property, an authority available under section 5(b) of the Trading with the Enemy Act which was not transferred to IEEPA. Its effect was to maintain the status quo with respect to Iranian Government assets held within the United States or by U.S. persons overseas on November 14. As required by IEEPA, the report of this action was immediately forwarded to Congress. And, at approximately 10 a.m. on that date, regulations implementing this order were filed at the Federal Register.

In general, the Treasury Department has sought to apply several basic principles in implementing the President's blocking order. First, we have sought to minimize damage to U.S. business interests. Thus, for example, we have issued both general and specific licenses authorizing Iranian entities to bring in "new", i.e., post-November 14, 1979, money to pay obligations to U.S. persons. Second, we have sought to avoid interfering with private remedies to the extent possible consistent with overall policy goals. We, therefore, quickly removed restrictions on the seeking of prejudgment attachments. Third, we have sought to provide the maximum guidance possible to the public as to how we intended to treat various types of transactions. This, for example, led us to publish numerous interpretations and general licenses when it became possible to articulate general rules.

More specifically, Executive Order 12170 of November 14, 1979, blocking Iranian Government property, has been implemented through the issuance of the following Treasury regulations:

- On November 14, 1979,\* Treasury adopted the initial Iranian Assets Control Regulations by blocking Iranian government assets.
- On the same date, Treasury amended those regulations to license U.S.-owned or controlled foreign firms such as overseas branches or subsidiaries of domestic banks, to set off their claims against blocked assets held by them outside the United States for Iran or Iranian entities.
- Also effective November 14, Treasury added general licenses to alleviate some of the hardships that might have been imposed on U.S. claimants by the blockage and to authorize shipments of certain blocked property such as food, clothing, medical supplies, and educational material.
- On November 19, 1979, Treasury added definitions, interpretations, general licenses, and procedures to the Iranian Assets Control Regulations.
- On November 23, 1979, Treasury amended the regulations to authorize judicial proceedings with respect to blocked accounts, up to but not including entry of judgment, and to make other changes.
- On November 28, 1979, Treasury amended the regulations to clarify, by the use of questions and answers, their effect on certain letters of credit.
- On November 29, 1979, Treasury amended the regulations to insulate specifically licensed Iranian property from attachments previously authorized by the regulations.
- On December 18, 1979, the regulations were amended to add definitions, set forth policy concerning the payment of checks and drafts, and for other purposes.
- On the same date, the regulations were amended to clarify previously announced rules and policies dealing with letter of credit situations.
- On December 26, 1979, certain rules were clarified regarding extensions of credit to Iran and the transfers of blocked accounts from demand to interest-bearing status at the instruction of the depositor.

\* These dates refer to the effective date of the regulations rather than the date they were filed or appeared in the Federal Register.



- Finally on January 7, 1980, the regulations were amended to clarify rules regarding the renewal of standby letters of credit and the treatment of letter of credit documents.

All of these regulations were intended to implement in a fair and equitable manner the President's order blocking Iranian Government property. Nonetheless, many special cases involving U.S. persons, Iranian Government entities and individuals, and other foreign governments and entities have been handled by specific licenses, which generally are issued when necessary to deal with special circumstances.

Although the blocking of the Iranian Government property severely affected trade between the United States and Iran, the November 14th Executive order and the implementing regulations did not contain an explicit prohibition on such trade where blocked property was not involved. However, the President decided to impose further economic sanctions against Iran following the rejection by the Iranians of further diplomatic efforts to secure the release of the hostages. Accordingly, on April 7, 1980, Executive Order 12205 imposed further prohibitions on certain transactions with Iran and its nationals. These prohibitions were those which the United Nations Security Council would have voted to impose on January 10, 1980, had they not been vetoed by the Soviet Union. The prohibitions announced on April 7 prohibited exports to Iran, except those involving food, medicine, medical supplies, and donations of clothing intended to be used to relieve human suffering, imposed restrictions on the shipment of goods to Iran and on new service contracts with Iran, and prohibited various financial transactions to which Iran or its nationals are a party. Treasury implemented this Executive order by filing regulations on April 7, 1980.

Finally, on April 17, 1980, the President signed Executive Order 12211 designed to further isolate Iran by adding new prohibitions. This order prohibits imports of goods from Iran or of Iranian origin merchandise, payments, or transfers of funds or other property to any person in Iran, and payments and transactions in support of travel to or maintenance in Iran of U.S. citizens and permanent resident aliens. News gathering activities in Iran were exempted from these prohibitions. In addition, the President ordered the revocation of various licenses previously issued to certain Iranian entities, thereby preventing them from maintaining offices here. Treasury implemented these prohibitions by regulations which were effective on April 17. In addition, on April 30, 1980, interpretative regulations relating to the various Executive orders were also filed.

Throughout this recent period of difficulties with Iran, the broad and discretionary powers of IEEPA have proved to be useful tools, enabling the President to swiftly protect U.S. interests while imposing economic sanctions against Iran in a deliberate manner, allowing the measures to complement parallel U.S. diplomatic and other pressures on Iran. Whether additional actions involving Iran under the authority of IEEPA will be necessary depends largely on future events. Treasury will from time to time, of course, issue additional regulations to implement existing sanctions.

At the President's direction, Treasury has also undertaken formal censuses of those assets blocked by the November 14th order and of the claims of U.S. nationals against Iran. Regulations providing for these censuses were filed on April 7 and impose reporting requirements with respect to blocked Iranian assets held by any persons subject to the jurisdiction of the United States between November 14, 1979, and March 31, 1980 as well as for claims by U.S. nationals against Iran and Iranian entities. The filing deadlines for forms on claims and assets is May 15, 1980. While the amount of blocked assets held by U.S. entities here and abroad is estimated to exceed \$8 billion, a more precise statement as to the amount of blocked assets and of potential claims must await analyses of the results of these censuses.

The imposition of extraordinary measures such as those taken here always raises many difficult issues, including their impact on international economic and monetary relationships. It is always important, therefore, that the economic and financial sanctions be used only when truly required by the circumstances. Unfortunately, this use continues to be required by the current situation.

**Exhibit 41.—Remarks by Secretary Miller, May 12, 1980, at dedication of plaque for Treasury officers killed in line of duty, in the Treasury Exhibit Hall, Washington, D.C.**

I would like to thank all of you for joining me on this very special occasion as we commemorate our Treasury agents killed in the line of duty.

I know such ceremonies have great significance to every law enforcement officer—local, State and Federal—because few members of any professional community enjoy the genuine concern for each other's welfare that law enforcement officers share.

But, I am sure that concerned citizens of *all* walks of life share the same emotional response when the words 'Officer Killed in the Line of Duty' appear in print.

We *all* know that there is no way to measure the scope of the tragedy because it diminishes not only the welfare of the officer's family, but the welfare of the community as well.

Since 1963, when President John F. Kennedy first set aside May 15th as the day to honor all peace officers killed in the line of duty, the world has changed dramatically. We have seen an increase in terrorism—an increase in the types of crimes and criminals confronting the law enforcement officer.

So as we pause 17 years later to commemorate these fallen colleagues, we are painfully aware of the difficulty peace officers encounter today in performing their mandate. We are particularly reminded of these problems this year as now another name has sadly been added to the list of those killed in the line of duty—Perry Watkins of the United States Secret Service.

Each name on this plaque is a vivid reminder of the necessity of law enforcement. And each name is proof of *their* contribution—in the most fundamental way—to the peace and stability of our society.

If, in pausing once a year to honor these dead, it reinforces our own sense of purpose, our own determination to preserve law and order, and our own awareness of how much these professionals, who protect us by day and night, need *our* support, then we have offered the ultimate tribute to their sacrifice.

**Exhibit 42.—Press release, May 20, 1980, U.S. Customs announces increased duty on unfinished trucks**

The U.S. Customs Service announced today that it will classify lightweight truck chassis with cab attached (cab chassis) as unfinished trucks rather than as chassis. The duty on unfinished trucks is 25 percent under items 692.02 and 945.69, Tariff Schedules of the United States (TSUS). The duty on chassis is 4 percent under TSUS item number 692.20.

Last year, \$1.5 billion worth of cab chassis were imported into the United States, mostly from Japan. In the past, cab chassis, which are trucks without the cargo boxes and which have limited cargo-carrying capacity, have been classified as "chassis."

Classification as chassis was supported by court decisions which held generally that the absence of a part that prevented an otherwise complete article from being used in the manner intended also prevented its being classified as the article itself. Because the absence of a cargo box in most cases prevented the cab chassis from being used in the manner intended, Customs determined that the cab chassis could not be classified as an unfinished truck.

However, a recent court case, *Daisy-Heddon, Div. Victor Comptometer Corp. v. the United States*, C.A.D. 1228 (1979), modified the principle previously used to determine whether an imported article was a "part of an unfinished article." This decision replaced the "essential part" test with a set of balancing tests in which value, number of parts, and labor in an imported article are compared to the value, number of parts, and labor to be added in the United States. Customs concluded that, based on this decision, cab chassis should be classified as "unfinished articles."

Notice of this change was sent to the Federal Register today, May 20, 1980. The ruling will become effective in 90 days.

Other classification rulings are also being reviewed in light of the court's decision.

**Exhibit 43.—Excerpt from statement of Assistant Secretary Davis, June 5, 1980, before the Senate Committee on Banking, Housing and Urban Affairs, on the Bank Secrecy Act**

**Cash flow study**

As part of our continuing efforts to improve the implementation of the Bank Secrecy Act, in 1979 the Treasury Department initiated a study of currency transactions at Federal Reserve offices throughout the United States. As the report of our findings indicates, it was undertaken "to gather information which would be useful in assessing the effectiveness of the existing reporting requirements and in identifying areas that appear to merit further study or investigation." The data covered the period 1970 through 1978 and showed a constantly increasing supply of currency in circulation. In 1978, for example, an additional \$10.2 billion was placed into circulation. Our analysis of the data highlighted at least two patterns which warranted additional investigation.

One of them, related to the currency transactions in Florida, would appear to be especially pertinent to the subject of these hearings. The Federal Reserve offices in Florida have consistently received more currency in deposits than they have placed into circulation, contrary to the national pattern. Since the end of 1974, however, there has been a startling acceleration in the amount of this surplus. The net receipts (surplus) have grown from \$921 million in 1974 to \$4.9 billion in 1979. And, it has already surpassed \$2.5 billion this year.

Although a variety of factors have contributed to the surplus, it is clear that a substantial amount is related to the trafficking in marijuana, cocaine, and other drugs in Florida. This conclusion is supported by information received from Customs, DEA, and other Government sources. The Treasury Department is working with the IRS, bank supervisory agencies, and the Justice Department in conducting followup inquiries about this matter.

A second pattern warranting additional attention involves the increase in \$100 bills in circulation. During the 1970 to 1978 period, \$100 bills have accounted for an increasingly large part of the annual increase in the Nation's supply of currency. In 1978, \$5.4 billion, more than 50 percent of the additional currency in circulation, was in \$100's. This represents a 410 percent increase over the \$1 billion added to circulation in 1970. Our analysis shows that the New York Federal Reserve office has accounted for a large part of the additional \$100's that are being put into circulation. This has been particularly noticeable since 1974. In 1978, for example, when the increase in \$100's was about \$5.4 billion, New York was responsible for almost half of it, \$2.6 billion. These figures are especially significant because some analysts believe that the increase in \$100's may be related to the growth of the subterranean economy. Followup studies concerning this situation are underway.

**Regulatory changes**

In order to enhance the usefulness of the Currency and Foreign Transactions Reporting Act, we have just amended the Treasury regulations governing the reporting of currency transactions. The amendments, which become effective next month, will—

(1) Control the ability to exempt regular customers from the reporting requirements. Banks are currently exempted from the reporting of currency transactions with an established customer maintaining a deposit relationship with the bank, in amounts which the bank may reasonably conclude do not exceed amounts commensurate with the customary conduct of the business, industry, or profession of the customer concerned. This requires the bank to exercise its professional judgment in determining whether or not a currency transaction report should be filed. The revision will require a record of the exemption to be made at the time it is granted and would limit the exemption to an established customer who operates a retail type of establishment within the United States; to a sports arena, racetrack, amusement park, bar, restaurant, hotel, or theater; to government agencies; and for payroll accounts in defined circumstances. Exemptions may not be granted to automobile and boat dealers. If the



customer is located in a contiguous or neighboring country, or if the business is not a retail establishment, a currency transaction report will be required.

(2) Provide additional assurance that this exemption is judiciously employed by the bank. A report listing the customers whose currency transactions are not reported because of the exemption is now required to be made to the Secretary of the Treasury or his delegate upon demand. The revision (1) specifies that the report shall include the name, street address, nature of the business, taxpayer identification number, and deposit account number of the customer whose transactions have been exempted under this provision; (2) elaborates on the Secretary's authority to remove a customer from the exempt list, and (3) requires the report to be submitted within 30 days after it is requested. These proposed amendments should provide the information Treasury needs in order to review the exemptions and to ensure that they are appropriate.

(3) Require banks to report transactions with, or originated by, financial institutions or foreign banks. Such transactions are currently exempt from the reporting requirement. The revision will limit this exemption to transactions with other domestic banks. Banks will be required to report large currency transactions with securities dealers, foreign banks, and miscellaneous financial institutions such as exchange dealers, persons in the business of transferring funds for others, and money order issuers. The additional information concerning the currency transactions with foreign banks and nonbank financial institutions will substantially improve the Treasury Department's ability to obtain overall compliance with the regulations and alert the Department to unusual transnational movements of currency.

Since Treasury presently does not receive reports of currency transactions between domestic and foreign banks, it cannot identify unusual movements of currency involving particular institutions or classes of institutions which might provide insights into possible criminal activities. The amendment will correct this deficiency.

The requirement that banks report transactions with securities brokers/dealers and other miscellaneous financial institutions will also provide an effective and badly needed check on the compliance of such institutions with the regulations. Such institutions, particularly those in the "miscellaneous" category, are much more difficult to recognize and catalogue than are banks. By requiring banks to report large currency transactions with such firms, the opportunity to identify those that are dealing in significant amounts of currency will be greatly increased. Once identified, they can be scheduled for compliance reviews.

(4) Require that a report be filed within 15 days after the day on which a transaction occurred instead of 45 days under the current regulations.

(5) Tighten the requirements for the identification of a customer involved in a large currency transaction, specify the documents that will be acceptable for identification, and require that the method of identification used be included in the report.

(6) Require financial institutions to retain a copy of each currency transaction report for a period of 5 years. While it is our understanding that many banks routinely retain copies of the reports, the requirement will ensure that copies will be available for the use of the bank supervisory agencies that have the responsibility for examining financial institutions for compliance with the reporting requirement.

The changes relating to exemptions are particularly important. Obviously, exemptions are necessary to eliminate the reporting of legitimate business transactions that would be of little or no interest to law enforcement officials. Banks were given this authority because it was thought that, due to their knowledge of their customers' financial activities, they would be able to identify such transactions without difficulty.

We have already asked approximately 1,000 banks in Florida, New York, California, and Illinois to provide us with their exemption lists. Our review of the lists of exempted customers that we have received from those banks confirms our previous view that there has been a great lack of understanding of the purpose of the exemption provision. Bank officials have exempted foreign nationals and other individuals from the reporting requirements solely on the basis that they have customarily brought in large amounts of currency. The bankers frequently had no knowledge of how that

currency was accumulated. We suspect, in some instances, that it was drug money. Our amendments are designed to deal with this problem.

### **Remedial legislation required**

In addition to the regulatory changes, certain legislative changes are needed to help us to deal more effectively with the activities associated with the movement of money by criminal elements. In particular, the Customs Service currently lacks sufficient authority under the Act to enforce the requirement that everyone who carries more than \$5,000 out of the country must file a report with Customs at the time he leaves the United States.

The best way to illustrate the problem is to contrast the situation the Customs Service faces in checking departing travellers with the situation when travellers are entering the United States.

Imagine an individual arriving by plane from abroad with \$10,000 in cash in his luggage. As he approaches the U.S. Customs inspector for routine inspection and clearance, he is notified of his legal obligation to file the Customs Form 4790 (Report of the International Transportation of Currency and Other Monetary Instruments) because a specific question concerning this obligation appears on the baggage declaration form given to him on the airplane. In addition, signs notifying travellers of this requirement are posted at ports of entry and verbal notice of the requirement may also be given by Customs personnel. Should the passenger attempt to avoid filing this form, it is conceivable that the currency would be discovered by the customs inspector in the course of the routine inspection. If the individual declines to file the report after being specifically advised of his obligation to do so, and the currency is discovered, there is no question that a violation of the Act has occurred. The individual has transported the currency into the United States without filing a report, and the customs inspector clearly had the authority to search his baggage. Further investigation can also be undertaken by customs agents to determine more about the underlying facts and, in particular, whether the funds were transported in furtherance of a violation of another Federal law. This is the easy case.

Imagine, however, a private airstrip in Florida, where a small private jet has taxied out on the runway as an impeccably dressed man carrying an attache case walks out to meet the plane. A customs officer, on the scene only because he had just received an anonymous phone call that someone was leaving for South America from that airport with \$250,000 in cash, stops the well-dressed man and asks where he is going. After the man indicates that he is going to Colombia, the customs officer asks if he is carrying more than \$5,000 in currency or monetary instruments and informs him of the reporting obligation. When the man responds in the negative, the customs officer opens the attache case and discovers that it is filled with \$100 bills.

Under current law, this person's failure to file may not produce a conviction. Although there is little doubt that within the next 5 minutes he would have been airborne, on a southerly course, with the unreported \$250,000, and beyond the reach of Federal law enforcement authorities, the subject had not yet departed from the United States when the customs officer stopped him. Some courts have held that it is not a violation of the Act to attempt to transport currency out of the United States without filing the report and/or that the actual violation does not occur until the individual has left the United States and is, therefore, beyond our jurisdiction.

This incident also dramatizes Customs lack of authority to verify the individual's negative response by opening the attache case. In this instance, the facts leading to the search may very well not constitute probable cause, the search standard in the Act, a standard I might add, which is not constitutionally mandated. Thus, even if there was a violation of the Act, the evidence may be suppressed. It is evident that under existing statutes the customs inspector has much greater authority to examine an incoming individual's luggage, which gives him a good opportunity to discover a violation of the currency-reporting requirement. Customs is, however, virtually powerless to enforce the Act with respect to departing travellers. This difference is particularly troublesome since the customs officer frequently will not have the opportunity to develop additional evidence before the suspect leaves the United States.



Another problem involves the lack of coverage at departure points. Customs personnel generally are not stationed at smaller airports or even at major departure points; they are at places of entry. There is no routine screening of individuals as they leave the United States. Therefore, to a very large degree we must rely on prior information to alert us to violations by departing travellers. We must develop sources of information concerning the financial operations of organized narcotics traffickers. To encourage people who have this sensitive information to contact the law enforcement community, it is, unfortunately, necessary to offer something valuable in return. Without an inducement, the potential informant will have little motivation to come forward, particularly considering the dangers involved for those who do.

Fortunately, Mr. Chairman, a bill introduced by you, S. 2236, would solve many of these problems. This bill is similar, in many respects, to H.R. 5961, introduced by Congressman LaFalce, which the Department has endorsed. It is our understanding that S. 2236 would make the following changes in Chapter 3 of the Act:

1. It would amend section 231(a)(1) by making it a crime to attempt to transport or "have transported" monetary instruments exceeding \$5,000, without complying with the reporting requirements.
2. It would amend section 232(a), relating to forfeitures providing that forfeitures of seized instruments shall apply in cases of failures to file only if there is a knowing failure to file. Provisions relating to forfeitures of instruments seized as a result of material omissions or misstatements remain unchanged.
3. It would amend section 235 by authorizing customs officers to stop, search, and examine without warrant, entering or exiting persons, vehicles, vessels, aircraft, containers, envelopes, and other conveyances where there is reasonable grounds to believe that they will be carrying unreported instruments.
4. It would add a new section 214, authorizing the Secretary to pay rewards, except to Federal officers and State and local officers acting in the furtherance of their official duties, for original information leading to the recovery of a criminal fine, civil penalty, or forfeiture exceeding \$50,000. It provides that the Secretary shall determine the amount of the reward but in no case shall it exceed 25 percent of the net amount of the fine, penalty, and forfeiture assessed, or \$250,000, whichever is less. There also is provision for necessary appropriations.

The "attempt" and "reward" provisions of S. 2236 and H.R. 5961 are the same and are supported by the Department. The proposal in S. 2236 to amend section 235 of the Act to permit warrantless searches incorporates a standard of "reasonable grounds to believe" reportable monetary instruments are being transported. We would prefer the language in H.R. 5961 which would establish a standard of "reasonable cause to suspect." While it is unclear whether the courts would interpret these two standards differently, the "reasonable cause to suspect" formulation of the Customs border search power has been specifically approved by the Supreme Court and we urge that it be used here.

The provision in S. 2236 to limit Customs authority to seize and forfeit unreported monetary instruments has not been included in other legislative proposals. While this proposal does reflect current policy, Customs requires a knowing violation before instituting forfeiture proceedings—we urge that this requirement not be included in the statute. To do so, we are concerned, would require the customs officer to determine the subjective intent of the violator before seizing the monetary instruments. Currently, the seizure is made at the border and then followup investigations, something which frequently will be impossible, determines whether any mitigation is appropriate.

We recognize that neither our regulatory changes and other efforts nor the proposed changes included in S. 2236 will totally prevent criminals from moving cash across our borders and through our banking system. They will, however, make the job of the criminal more difficult, exposing them and their allies to increased risks of prosecution and of substantial monetary penalties. This would involve a substantial improvement in our enforcement effectiveness. We therefore urge this Committee to support S. 2236.



**Exhibit 44.—Press release, June 3, 1980, Treasury Department tightens regulations on reporting of unusual currency transactions.**

The Treasury Department today tightened the requirements for the reporting of large currency transactions.

The changes, which take effect 30 days after publication in the Federal Register, amend Treasury regulations issued under the Bank Secrecy Act that require financial institutions to report unusual currency transactions in excess of \$10,000.

The new regulations (1) restrict the ability of financial institutions to exempt customers from the reporting requirements; (2) remove existing exemptions from the reporting of large currency transactions by securities dealers, foreign banks, and miscellaneous financial institutions such as dealers in foreign exchange, persons in the business of transferring funds for others, and money order issuers; (3) require reports to be filed within 15 days after a currency transaction takes place; (4) require more complete identification of a person dealing in large amounts of currency; and (5) require retention of a copy of the report for 5 years.

Transactions with an established customer maintaining a deposit relationship are currently exempt from the reporting requirement. The amendment limits this exemption to certain domestic businesses and requires that the location and nature of the business be identified in the report of exempt customers furnished to Treasury.

The amendment of the reporting requirements is one of the measures the Treasury Department proposed last year after discovering that banks were depositing extremely large amounts of currency in the Federal Reserve bank offices in Florida. The changes are expected to improve the effectiveness of the currency-reporting provisions and provide valuable information concerning currency from illegal transactions and previously unreported flows of currency in the United States.

Proposed amendments to tighten reporting requirements were published by Treasury in September 1979. A total of 46 comments were received on this proposal and each was thoroughly considered from the standpoint of overall effectiveness, practical limitations and the purpose and objectives of the statute. As a result, a number of the proposals were substantially modified before their adoption.

A copy of the amendments can be obtained from the Treasury's Office of Public Affairs.

Notice of this action was published in the Federal Register on June 5, 1980.

**Exhibit 45.—Statement of Assistant Secretary Davis, September 15, 1980, before the Subcommittee on Constitution of the Senate Committee on the Judiciary, on enforcement operations of the Bureau of Alcohol, Tobacco and Firearms**

I am appearing here today to discuss with you various aspects of the operations of the Bureau of Alcohol, Tobacco and Firearms. As the Assistant Secretary for Enforcement and Operations, I have oversight and general supervisory responsibility for five Treasury entities which have enforcement responsibilities. They are the U.S. Customs Service; the U.S. Secret Service; the Office of Foreign Assets Control; the Federal Law Enforcement Training Center; and the Bureau of Alcohol, Tobacco and Firearms. I also am responsible for coordinating law enforcement policy for the Treasury Department.

As part of my responsibilities, I am necessarily concerned with the agency priority-setting process, methods and practices of operations, and, of course, allegations of misconduct and abuse. I wish to discuss very broadly certain policies of the Treasury Department which are relevant to these hearings and how the Bureau of Alcohol, Tobacco and Firearms has sought to implement these policies.

In discussing the activities of law enforcement agencies, it is useful initially to articulate several underlying premises. First, criminal, and frequently regulatory, investigations are by their nature conflict oriented. As a consequence, it is not unusual for such inquiries to produce negative reaction from the subjects of investigation. This is often the case regardless of guilt or innocence. The relationship of investigator or prosecutor and possible violator is simply not the kind of relationship which creates good feeling among the parties involved.

Second, the rigorous enforcement of violations of the criminal laws, which is often a necessary ingredient to the effective accomplishment of an agency's mission, can sometimes lead to instances of abuse or misconduct on the part of the investigator. Any law enforcement official who says that in their agency there will never be a case in which an agent does something that is inappropriate is being naive. At the same time criminal investigations, by their nature, can produce false allegations of misconduct or other wrongdoing from the subject of an investigation.

Third, when an investigation is commenced, it is not always known whether the person being investigated is actually guilty. It is the function of the investigation and, where indictment follows, of the trial ultimately to determine whether someone is guilty of a criminal violation.

The existence of these premises which define the real world in which an agency operates does not mean that instances of possible misconduct or unwise action should be accepted as inevitable. To the contrary, it is vital that those managing enforcement agencies aggressively act to minimize their occurrence. To do so, among other things, it is important that internal affairs capabilities be improved; that clear policies, particularly in areas of controversy, be developed; that program goals be articulated; and that management systems be developed adequately to monitor agency performance. Treasury and BATF have taken actions in all these areas during this administration. The steps taken are described in statements submitted by Director Dickerson in connection with other recent hearings. They are attached for your reference.<sup>1</sup> I will summarize what has been done.

Two principal actions have been taken to enhance internal affairs capabilities. First, though not required to do so by statute, Treasury created an Inspector General to provide oversight for and leadership of all internal affairs operations in the Department. Second, last year I approved Director Dickerson's major reorganization of the Bureau's Office of Internal Affairs which should make it substantially more effective. In addition, in order to make certain that we are aware of individual incidents of misconduct or patterns which may need special attention, I formally asked the Justice Department to notify the relevant Treasury law enforcement agency whenever a motion to suppress is granted on account of the actions of one of its agents or when a court finds that an agent committed illegal or otherwise improper acts.

Numerous changes in policy have also been made by BATF to provide clearer rules for its personnel and to improve its internal management. These include:

- Reorganization of the Office of Criminal Enforcement on October 1, 1979, into a regional structure so as to provide closer supervision over enforcement operations.
- Unannounced inspections of licensed firearms dealers have been limited to exceptional circumstances.
- Priority was given to regulatory as opposed to criminal enforcement at gun shows wherever possible.
- A comprehensive national firearms policy has been developed. ATF resources are now targeted against substantial and/or repeated suppliers of criminal guns and other major Federal violators.
- The use of the "straw man" investigative technique has been limited.
- Guidelines have been promulgated concerning the handling and ultimate disposition of firearms seized by the Bureau.
- Stringent standards have been set for cases in which administrative action is sought following failure of criminal prosecution.
- Guidelines have been developed to limit the number of firearms seized to those clearly involved in the violation.

BATF is also seeking to determine whether regulatory and other policy changes are appropriate. For example, public comment has been sought on the desirability of allowing firearms licensees to sell at gun shows; on whether a more precise definition of "engaged in the business" can be developed; and on whether BATF should use suspension of licenses as an alternative to revocation or nonrenewal. All of these regulatory projects were commenced in response to criticisms about the manner in

<sup>1</sup> Not included in this exhibit.

which BATF was enforcing the law. In addition, BATF is currently exploring the possibility of removing those weapons which have a high degree of collector appeal from the classification as destructive devices.

Enforcement of the law is a difficult job. In many areas, it produces controversy. Unfortunately, this is particularly true where firearms are concerned. Nonetheless, our policy and our goal remains to enforce the law so as to meet its underlying objective—to limit the criminal acquisition and misuse of firearms. In doing so, we will be firm but we will also seek to be fair, to minimize to the extent possible incidents of misconduct, and to enforce the law in a sensible and sound manner.

## Tax Policy

### **Exhibit 46.—Statement of Secretary Miller, October 22, 1979, before the Subcommittee on Taxation and Debt Management of the Senate Finance Committee, on restructuring the system of depreciation allowances**

Thank you for inviting me to discuss S. 1435, a very significant proposal to restructure the system of depreciation allowances. I am pleased to see the broad interest in legislation to encourage capital formation and increase productivity.

The 10-5-3 proposal would restructure the system of tax allowances for capital recovery. It would greatly shorten the periods over which most capital expenditures can be written off. The proposal provides for nonresidential buildings to be written off over 10 years, in a pattern so accelerated that 70 percent of the acquisition cost could be deducted in the first 5 years. Expenditures for most machinery and equipment could be fully written off, also in an accelerated pattern, over 5 years. A limited amount of expenditures for cars and light trucks used in businesses would be written off over a 3-year period.

This proposal would also liberalize the investment tax credit, by allowing the full 10-percent credit (instead of 6⅔ percent) for equipment depreciated over 5 years, and a 6-percent credit (instead of 3⅓ percent) for the 3-year class of assets. A phase-in over 5 years is proposed whereby the writeoff periods, starting from a 1980 base, are reduced year by year. The 1980 lives are determined by reference to the current asset depreciation range (ADR) system. Advocates of 10-5-3 argue that it would promote simplification and certainty, aid small business, and provide incentives for capital expansion. These are laudable goals, and should be considerations in evaluating any tax structure. Evaluation of our current system shows that there is room for improvement.

### **Economic background**

The increase of 2.4 percent in real GNP for the third quarter of this year is further indication of strength in the economy, but prices continue to show rapid increase. I want to emphasize that the administration intends to sustain a firm and consistent policy to reduce inflation. This policy has a number of aspects, but none is more important than the maintenance of strict fiscal discipline. At the present time, the action of steady budget pressure to slow the rate of inflation offers the strongest promise of restoring the health of our economy, reducing economic uncertainty, and reversing expectations for future inflation.

I believe that a commitment to widen the budget deficit by the magnitude of S. 1435 would be premature at this time. However, we should study possibilities for a program that will promote longer range economic objectives as effectively and fairly as possible. At the appropriate time, you should be prepared to act on a program carefully structured to expand economic capacity, to reduce production costs, and to promote productivity. Appropriate depreciation allowances can help to accomplish these goals and should be given serious consideration as an element of any future tax package.



### Revenue costs of 10-5-3

Looking specifically at the 10-5-3 proposal, I would first point out that it would have a massive budget impact. The cost of S. 1435 rises from about \$4 billion in the first year to over \$50 billion in 1984 and over \$85 billion in 1988 (see table 1).

These estimates have been carried out further into the future than we would normally show in order to see the full effect of the proposed phase-in rules. Because the program would be implemented gradually during the first 5 years, it is not until 1984 that the full benefit of the more liberal depreciation allowances would be given to investment for any one year. For this reason, the revenue costs continue to build until 1988, after which revenue losses begin to fall. Eventually, the level of these losses stabilizes and thereafter they grow at about the same rate as investment expenditures. By 1987, when corporate tax receipts are expected to be \$116.7 billion, S. 1435 would provide corporate tax reduction of nearly half that amount. The total revenue cost also includes a reduction in individual income taxes resulting from deductions taken by unincorporated businesses. This is equal to about 15 percent of the total revenue cost.

The year-by-year revenue costs do not take account of the additional tax receipts resulting from economic expansion induced by the tax reductions. These "feedback" revenues amount to about 30 percent of the static revenue loss and are reflected primarily in increases in individual tax receipts. If these feedback revenues are taken into account, the result is a net revenue loss of about \$35 billion in 1984. It should be noted that the additional tax receipts that would be induced by this tax cut are about the same as that from any tax reduction having a comparable impact on GNP.

### Background on depreciation allowances

The present tax depreciation system is cumbersome and complex. It involves a number of choices and uncertainties, and is especially burdensome for small businesses. It should be simplified. The present system provides an insufficient incentive for capital expansion in periods of rapid inflation and financial uncertainty. These incentives should be strengthened as much as our budget resources will allow.

Under the present rules, the business taxpayer is confronted with a myriad of choices. The first choice is whether to use the ADR system or to justify tax allowances on taxpayer's particular facts and circumstances. For those electing ADR, there is a choice of useful life within the allowable range for each class of assets. For all taxpayers there is also a choice of depreciation methods over the chosen lifetime. For some types of assets, especially buildings, there may be no ADR class and there may be a restricted choice of methods. With regard to types of equipment having allowable lives less than 7 years, the taxpayer must choose whether to forsake some portion of the investment tax credit in favor of more rapid writeoff. For large firms having computerized accounting systems, these options present no formidable problems. They elect ADR, using the most rapid method of depreciation, and the shortest available useful life after taking account of the investment credit rules. These large firms own the great bulk of depreciable assets.

A very small percentage of small business taxpayers have chosen to elect the ADR system. Despite recent changes in regulations to reduce requirements for reporting, small businesses apparently believe that ADR dictates a more complicated accounting system and involves more complex regulations. If these small businesses choose not to elect ADR, but to use the shorter lives that are allowed without question to ADR electors—and we believe many small businesses so choose—they face the possibility that upon audit they may be required to justify those lives on facts and circumstances. For these reasons, small businesses may regard the ADR system as not addressed to their needs and circumstances.

### Productivity and investment

The stimulation of investment and improvement of productivity performance must be among the foremost objectives of economic policy. The share of business fixed investment in GNP has varied around a nearly flat trend for about the last 15 years (chart 1). However, in the last expansion it neither grew as rapidly nor reached as high a peak as during the previous cycle that peaked in 1974. Investment in nonresidential

TABLE 1.—*Revenue Estimates*  
[\$ Billions]

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
	Change in Tax Liability—Calendar Years									
Corporate...	-3.2	-8.5	-17.9	-29.9	-44.1	-57.2	-67.6	-72.9	-73.3	-70.9
Individual...	-0.6	-1.5	-3.2	-5.3	-7.8	-10.1	-11.9	-12.9	-12.9	-12.5
Total.....	-3.8	-10.0	-21.1	-35.2	-51.9	-67.3	-79.5	-85.8	-86.2	-83.4
	Change in Receipts—Fiscal Years									
Corporate...	-1.5	-5.6	-12.7	-23.3	-36.2	-49.8	-61.7	-69.8	-73.0	-72.1
Individual...	-0.2	-0.9	-2.1	-4.0	-6.2	-8.7	-10.8	-12.3	-12.9	-12.8
Total	-1.7	-6.5	-14.8	-27.3	-42.4	-58.5	-72.5	-82.1	-85.9	-84.9

structures has shown a persistent downward trend since 1966, while the equipment component has tended to increase as a percentage of GNP. This is partly explained by mandated expenditures for pollution control equipment, which are now about 7 percent of equipment spending.

Aggregate productivity growth has exhibited a pronounced decline in the last decade and output per hour worked is now well below its post-war trend (chart 2). For the 20 years ending 1968, the annual rate of growth in output per hour worked was about 2 ½ percent. More recently, and beginning even before the oil embargo and the recession of 1974 and 1975, the rate of this productivity growth has markedly slowed. In the years 1968 through 1973 the growth rate was only about 1 ¼ percent.

In the last recovery cycle, the upturn in productivity growth that normally accompanies expansion occurred later and was generally weaker than in other post-war recoveries (chart 3). The average for this latest period, 1973-78 was an annual productivity gain of only 1 percent. This slowing of productivity growth has helped to perpetuate a spiral of inflationary wage/price adjustments in the economy and has eroded our ability to compete in international markets.

While the recent growth in average productivity throughout the economy is unmistakably lower in recent years, this record is by no means uniform across major productive sectors (see chart 4). The communications sector has experienced rapid and even accelerating growth in productivity throughout the period, while at the other extreme, the construction industries have suffered declines in productivity in absolute terms since the late sixties, particularly over the most recent years. Among the public utilities, productivity growth has also slowed markedly since the late 1960's after rapid and steady increases up to that time. The record in manufacturing also shows a decline in the productivity growth throughout the 1970's but that growth has continued up to the present time, except for a 1-year downturn in 1974. In the trade sector, output per hour has grown at less than a 2-percent annual rate over the entire period and is nearly flat in recent years.

Within the manufacturing sector, productivity growth has been and continues to be somewhat stronger in nondurables manufacturing as compared to the durables sector (see chart 5). Among the durable goods industries the record of the motor vehicle industry has been particularly strong since 1974, while a pronounced decline in productivity has occurred in that same period for the primary metals industry.

The wide diversity in productivity gains across sectors and industries illustrates the importance of looking behind the aggregate trends. To the extent that declines in productivity in particular sectors can be attributed to lagging capital formation, we should pay close attention to the distribution of tax incentives among sectors of the economy, in addition to the aggregate amount of incentive. This is not to suggest that we attempt to direct all of the tax relief to particular industries that have poor productivity records (or those that have performed well) in the recent past but we should know the degree to which any proposal matches the incentives to the economic objectives.

Acceleration of depreciation allowances can be effective in providing investment stimulus. The direct tax savings that accompany the acquisition of capital provides additional cash flow to business firms for further investment and replacement. It is as if interest-free loans from the government were provided in the early years of a capital asset's use to be repaid out of the future productive output of these assets. These accelerated deductions reduce the "tax wedge" that is interposed between the returns to the physical investment and the rewards that can be paid to those who supply funds for investment. The reduction in the tax wedge reduces the cost of capital and, thereby, increases the amount of capital that can be profitably employed for the benefit of the company, its employees, and its customers.

### **The concept of capital recovery**

Before I get to a specific analysis of some of its likely consequences of the 10-5-3 proposal, I would like to discuss briefly the concept of capital recovery allowances. Many people regard depreciation as an arcane topic involving "useful lives," complicated formulas such as double declining balance and sum-of-years digits, vintage accounting, and numerous other technicalities. Although the subject of



depreciation is replete with imposing terminology, the underlying concept is straightforward. Depreciation is a cost of employing capital; as such, it must be deducted to arrive at net income, the same way that a wage deduction is taken for payments for labor.

In order to impose a tax on net income, the timing of receipts and expenses must be matched, and this requires that the cost of assets be deducted as they are consumed by use in a business. The Internal Revenue Code provides that there shall be a reasonable allowance for exhaustion, wear and tear, and obsolescence.

Of course, the determination of capital recovery allowances in any tax system is more difficult than for wage deductions because there is no current payment that measures the exact amount of capital consumed from one year to the next. The cost of depreciation each year is, therefore, estimated to be some proportion of the acquisition, or historical, cost of the asset. Inflation, however, increases capital consumption as measured in current dollars, and, therefore, depreciation allowances based on historical cost may be inadequate. Acceleration of tax depreciation may compensate for the general understatement of depreciation.

If the allowable depreciation deduction is greater for any year than the amount of capital consumed, the Government is in effect extending an interest-free loan to the business. In the opposite case, inadequate depreciation allowance will prematurely increase taxable income, impose prepayment of taxes, and reduce internal cash flow.

### **The effects of 10-5-3**

The 10-5-3 proposal is a major departure from current practice in the determination of depreciation or capital recovery allowances. It would allow a large share of the acquisition cost of equipment and structures to be deducted for tax purposes much more rapidly than currently. The proposal deals with the problem of complexity by substituting a single mandatory system in place of the existing complex of choices. The proposed system has simple categories, certain recovery periods, and a fully prescribed pattern of recovery allowances. This approach to both investment incentives and simplification deserves consideration, but there are deficiencies that should be examined carefully.

For example, the proposal is not as simple as it first appears. As drafted, the 10-5-3 proposal would have to establish mandatory guidelines lives during the 5-year phase-in that are tied to the ADR classification system. Each year, for 5 years, every taxpayer would apply a new schedule of depreciation rates to assets acquired in that year until they are fully written off. The phase-in rules also create a perverse incentive effect that postponement of investment until the following year will increase the rate of capital recovery allowances. The phase-in is intended to postpone the revenue losses, but it also increases complexity and uncertainty. To the extent that investment is delayed, feedback revenues are also delayed.

When the 10-5-3 rules are fully effective, their combination of rapid writeoffs of and increased investment credit for machinery and equipment would be very generous indeed. The investment credit would immediately pay for 10 percent of the cost of acquiring new equipment. Then 76 percent of the gross cost could be written off in the first 3 years; the entire amount in 5 years. The present value of the tax saving from the combination of the investment credit and the accelerated deductions is greater than full, first-year writeoff would be. The treatment of equipment under 10-5-3 would be better for the taxpayer than immediate expensing.

Such a dramatic increase in capital allowance is not only expensive in terms of the budget, but it could also greatly increase tax shelter activity. The proposed deductions and credits would be most attractive to high-income individuals who could obtain the tax benefits through net leasing of machinery and equipment. Tax shelter opportunities could also increase for those investing in buildings such as offices and shopping centers, as the proposed bill both shortens the recovery period for these buildings and accelerates the depreciation method. A tougher recapture rule for buildings is proposed in the bill, but this only offsets a portion of the potential tax-shelter benefits.

Another result of 10-5-3 is a wide range of differential benefits among businesses according to the types of assets that they use and their present industry classification. For example, machinery and equipment (other than automobiles and light trucks) are

TABLE 2.—“Best Allowable” ADR depreciation periods as compared to 10-5-3, selected industries

Asset class	10-5-3		ADR					
	All industries		All industries	Construction	Motor vehicles	Communication	Primary metals	Utilities
Autos and light trucks ..	3		3.5	3.8	3.1	4.4	3.2	4.5
Other machinery and equipment.....	5		10.2	5.1	5.8	14.6	11.3	20.4
Buildings .....	10		32.6	35.0	35.0	36.0	35.0	35.0
Total.....	5.9		12.7					

now depreciated as if they had an average depreciation lifetime of 10.2 years (table 2); the recovery period prescribed in S. 1435 is less than half that current average. For buildings, present practice is equivalent to an average lifetime of 32.6 years. The proposal would allow these buildings to be written off in less than one-third that time. For autos and light trucks, the reduction is relatively small from 3.5 years to 3.0 years although, in many cases, autos and trucks would benefit from an increase in the investment credit.

The variation in benefits provided by 10-5-3 is most pronounced when industry categories are compared. After the 5-year phase-in, all major industry classes would have higher depreciation allowances under 10-5-3. However, the share of projected total investment "paid for" by accelerated depreciation is generally higher for those industries employing longer lived assets. For machinery and equipment, you can see (table 2) that the reduction in the recovery period is minimal in the case of construction and very small for manufacture of motor vehicles. Toward the other end of the spectrum, the recovery period for assets used in the primary metals industry would be nearly half the present ADR lives, communications would be about one-third, and public utilities about one-fourth. (table 3 attached to this statement provides quarter industry detail.)

The Treasury Department has simulated changes in depreciation periods, together with the changes in the investment credit, to estimate potential tax savings during the period of phase-in. These estimates are then used to compute the tax saving per dollar of projected investment. Not surprisingly, the relative magnitudes generally follow in the same order as the degree of reduction in writeoff periods (chart 6). In 1984, the tax saving per dollar of projected investment in the construction industry would be less than 5 percent; for motor vehicles it is 8 percent; for primary metals it is around 15 percent; for communications just less than 20 percent; and the tax saving would pay for more than 20 percent of investment in the public utilities.

TABLE 3.— "Best allowable" depreciation life (years) under present law, by industry

	Cars and light trucks	Machinery and equipment	Building
All industries .....	3.5	10.2	32.6
Agriculture .....	3.9	7.7	20.0
Construction .....	3.8	5.1	35.0
Oil and gas:			
Drilling .....	3.2	7.0	35.0
Production .....	3.2	11.0	35.0
Refining .....	3.4	12.4	35.0
Marketing .....	—	13.0	13.0
Mining .....	3.6	7.8	35.0
Manufacturing:			
Food .....	3.2	9.2	35.0
Tobacco .....	3.3	11.4	35.0
Textiles .....	3.2	8.1	35.0
Apparel .....	3.1	7.1	35.0
Logging/sawmills .....	3.9	6.8	35.0
Wood products .....	3.8	7.1	35.0
Pulp and paper .....	3.2	9.9	35.0
Printing and publishing .....	3.1	8.7	35.0
Chemicals .....	3.1	7.7	35.0
Rubber products .....	3.1	9.6	35.0
Plastic products .....	3.0	8.0	35.0
Leather .....	3.0	8.5	35.0
Glass .....	3.0	9.2	35.0
Cement .....	3.5	14.0	35.0
Stone and clay products .....	3.5	10.9	35.0
Primary metal .....	3.2	11.3	35.0



TABLE 3.— "Best allowable" depreciation life (years) under present law, by industry—Con.

	Cars and light trucks	Machinery and equipment	Building
Fabricated metal .....	3.1	4.9	35.0
Machinery .....	3.0	7.9	35.0
Electrical machinery .....	3.0	9.3	35.0
Electronics .....	3.0	7.1	35.0
Motor vehicles .....	3.1	5.8	35.0
Aerospace .....	3.0	7.8	35.0
Shipbuilding .....	3.3	9.7	35.0
Railroad equipment .....	3.3	8.8	35.0
Instruments .....	3.1	9.0	35.0
Other .....	3.1	9.0	35.0
Transportation:			
Rail .....	—	11.7	—
Air .....	—	9.4	35.0
Water .....	—	15.7	35.0
Highway .....	3.4	5.6	35.0
Communication .....	4.4	14.6	36.0
Utilities:			
Electric .....	4.5	20.5	35.0
Gas .....	4.5	23.1	35.0
Pipeline .....	—	17.5	35.0
Wholesale and retail trade .....	3.5	6.8	35.0
Services .....	3.3	7.8	35.0
Amusements .....	3.0	9.8	35.0

Note: The "best allowable" depreciation period for an industry is a special type of weighted average of the best available depreciation periods (taking account of the investment credit effects of lives lower than 5 or 7 years) for equipment used in the industry. The weights are estimated 1976 investment in the several types of equipment. The weighted average takes account of the time value of tax saving. In the case of buildings not covered by ADR, the best available depreciation period is assumed to be 35 years, which is approximately the average useful life employed by taxpayers, as revealed by Treasury Department surveys in 1972 and 1973.

You may wonder about the apparent revenue increase in motor vehicle manufacturing for 1981. This results from a phase-in rule that immediately increases the recovery period for the auto companies special tools from 3 years up to 5 years. In later years, the year-by-year reduction prescribed for longer lived assets becomes dominant.

Highway transportation, services, agriculture, wholesale and retail trade, fabricated metals, and electronics are among other industries with relatively smaller benefits (table 4). Among the other larger gainers are railroads, shipping, and oil pipelines.

The benefits estimated here are "potential" in the sense that no allowance is made for the possibility that certain companies will have insufficient tax liabilities against which to take the full amount of any additional deduction. Likewise, the estimates for public utilities take no account of the rule that disallows the use of 10-5-3 to utilities that "flow through" the benefits of accelerated depreciation to consumers.

TABLE 4.— *Estimated tax reduction due to 10-5-3 as a percent of projected investment,<sup>1</sup> 1984*

Industry class	Estimated 1984 tax reduction	Projected 1984 investment	1984 tax reduction as percent of investment
	(\$ millions)	(\$ millions)	(Percent)
Manufacturing:			
Nondurables .....	5,729	50,016	11.5
Food .....	1,258	10,624	11.8
Tobacco .....	50	369	13.6
Textiles .....	332	2,757	12.0
Apparel .....	121	1,196	10.1
Pulp and paper .....	837	7,777	10.8
Printing and publishing .....	341	3,390	10.1
Chemicals .....	2,345	19,838	11.8
Rubber .....	123	927	13.3
Plastics .....	303	2,918	10.4
Leather .....	16	220	7.3
Durables .....	5,606	51,496	10.9
Wood products and furniture .....	98	2,100	4.7
Cement .....	90	622	14.5
Glass .....	146	1,258	11.6
Other stone and clay .....	281	2,150	13.1
Ferrous metals .....	1,107	6,739	16.4
Nonferrous metals .....	421	3,004	14.0
Fabricated metals .....	504	6,587	7.7
Machinery .....	950	8,345	11.4
Electrical equipment .....	493	4,448	11.1
Electronics .....	266	2,884	9.2
Motor vehicles .....	458	5,716	8.0
Aerospace .....	182	1,591	11.4
Shipbuilding .....	169	1,534	11.0
Railroad equipment .....	17	129	13.2
Instruments .....	222	2,383	9.3
Other manufacturing .....	202	2,006	10.1
Transportation .....	4,048	40,504	10.0
Railroads .....	562	3,362	16.7
Airlines .....	814	6,175	13.2
Water transport .....	1,432	9,492	15.1
Highway transport .....	1,240	21,475	5.8
Communication .....	5,956	32,130	18.5
Utilities .....	9,162	42,187	21.7
Electric utilities .....	7,533	35,853	21.0
Gas utilities and pipelines .....	1,629	6,334	25.7
Mining, except oil and gas .....	1,120	10,796	10.4
Oil and gas drilling .....	238	2,945	8.1
Oil and gas production .....	5,079	38,390	13.2
Petroleum refining .....	1,207	8,785	13.7
Petroleum marketing .....	142	1,254	11.3
Oil pipelines .....	2,202	10,175	21.6

TABLE 4.— *Estimated tax reduction due to 10-5-3 as a percent of projected investment,<sup>1</sup> 1984—Continued*

Industry class	Estimated 1984 tax reduction	Projected 1984 investment	1984 tax reduction as percent of investment
	(\$ millions)	(\$ millions)	(Percent)
Construction .....	1,114	25,085	4.4
Wholesale and retail trade .....	3,823	44,097	8.7
Agriculture .....	2,069	27,220	7.6
Services .....	3,337	41,109	8.1
Grand total .....	51,912	435,725	11.9

<sup>1</sup>Estimates of investment by purchasing sector are based on Annual Survey of Manufacturers, 1976, and data from regulatory agencies, trade associations, and other industry sources.

Among industries with relatively poor productivity performance over the last 5 years, the construction industry has the smallest amount of potential benefit from 10-5-3 among all industries and utilities has the largest (chart 7). Looking at the stronger productivity sectors, communication is among the larger gainers from 10-5-3, while communications and motor vehicles are among the more modest beneficiaries. In general, there is no discernible relationship between the amount of additional capital formation incentive provided by 10-5-3 and the relative strength of productivity performance over the past 5 years. The point here is not that these should be exactly matched, but rather that it is very difficult to see any purpose to the vastly different amounts of investment incentive provided across industries by 10-5-3.

I do not come to you today with any specific proposal nor, in view of the deficiencies of 10-5-3, can I support S. 1435. I am obviously concerned about the large revenue cost, and the implication that greatly differing amounts of investment stimulus would be scattered about indiscriminantly among industries and asset types.

The simplification objectives of 10-5-3 could be achieved through other depreciation proposals. I would further suggest that you should consider the continuation of some administrative mechanism for the system to assure that the capital recovery deductions allowed for tax purposes are consistent with changes in true depreciation costs. I believe we should analyze carefully a wide range of depreciation plans, and I will continue to develop and work with you to promote a depreciation or capital recovery system that we can all regard as simple, effective, and fair. Such a system should be put into effect as soon as budgetary resources and prudent fiscal policy permit.



Chart 1

# BUSINESS FIXED INVESTMENT AS PERCENT OF REAL GNP

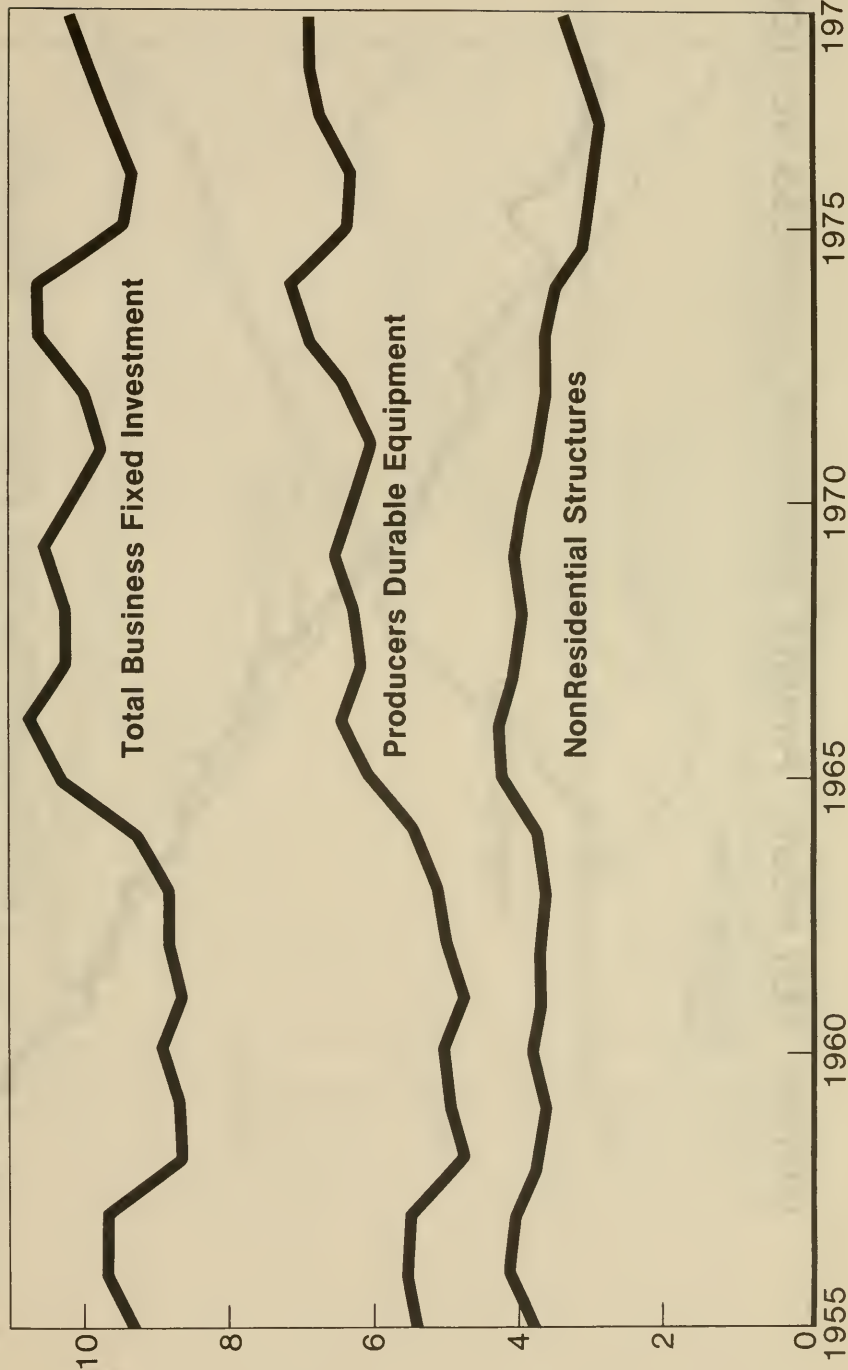
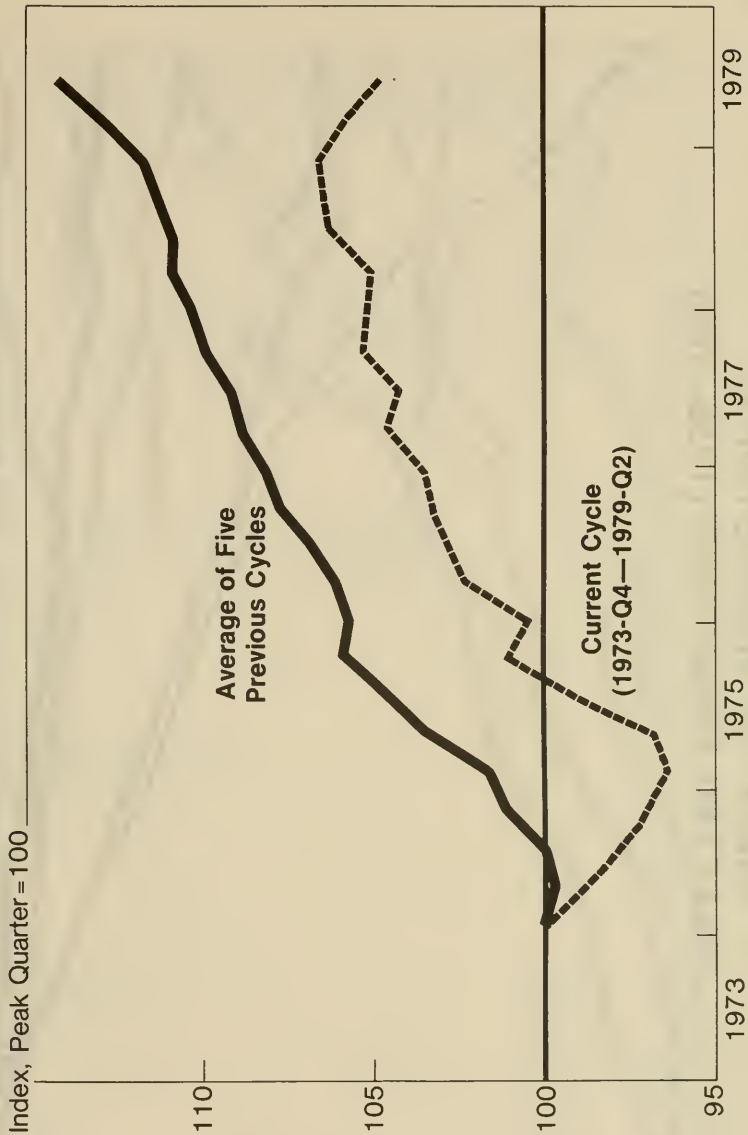


Chart 2

# OUTPUT PER HOUR, PRIVATE NONFARM BUSINESS SECTOR



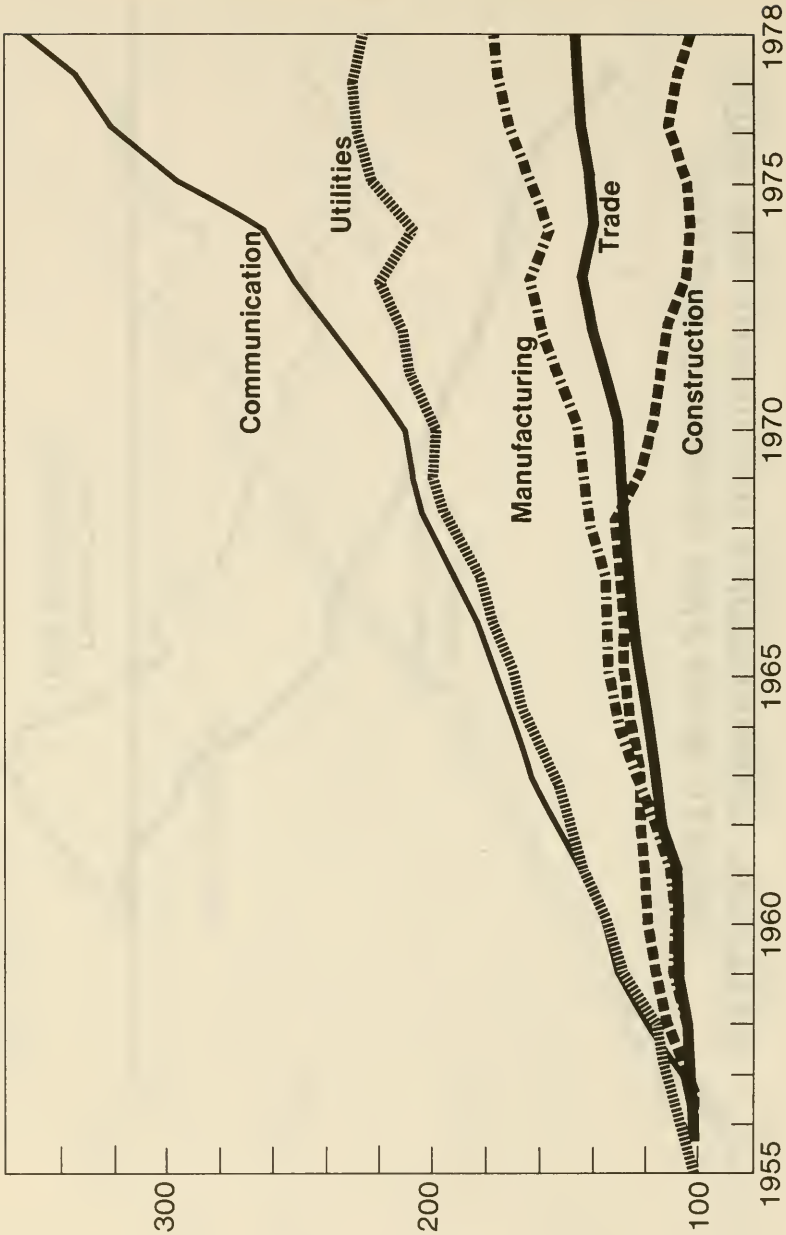
Chart 3  
**CYCLICAL COMPARISONS OF OUTPUT PER HOUR,  
PRIVATE NONFARM BUSINESS SECTOR\***



\*Changes following the cyclical peaks as specified by NBER.



Chart 4  
**INDEX OF PRODUCTIVITY,  
SELECTED INDUSTRIES (1955=100)**



# INDEX OF PRODUCTIVITY, SELECTED MANUFACTURING INDUSTRIES (1955=100)

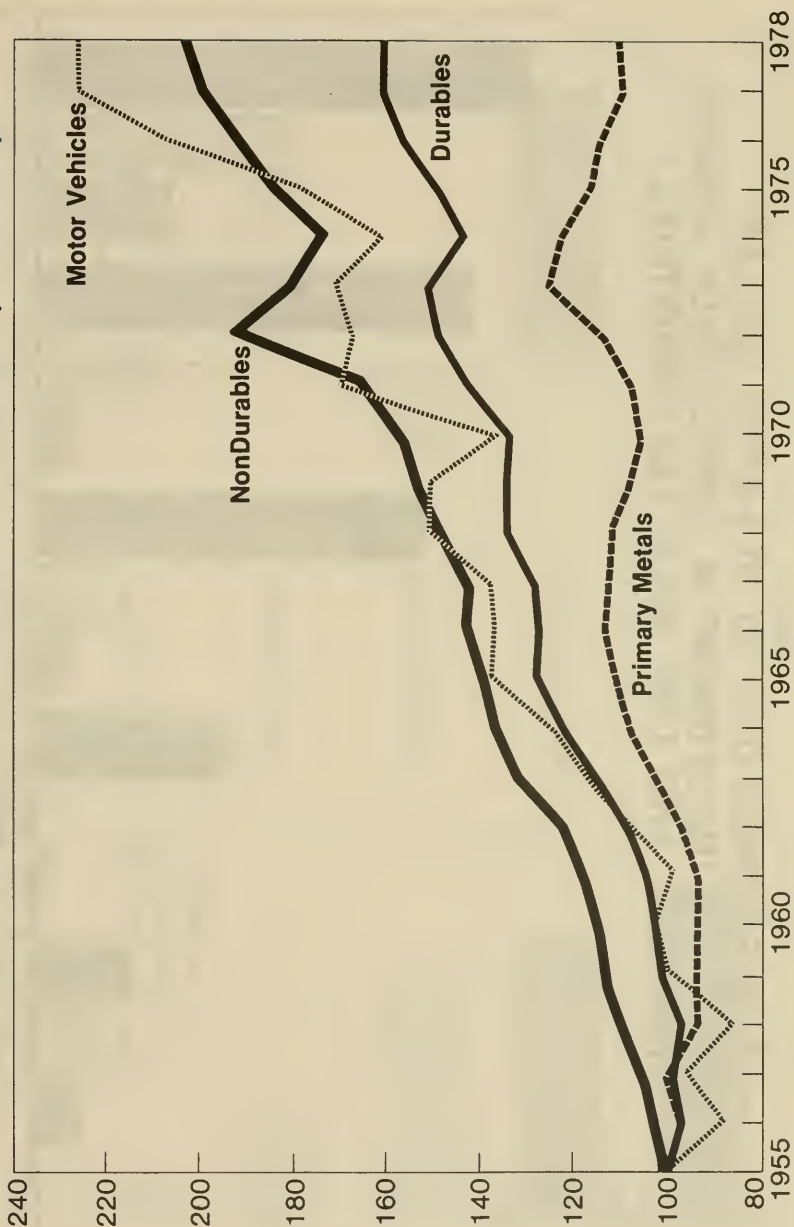


Chart 6

# **TAX SAVINGS DUE TO 10-5-3 PER DOLLAR OF PROJECTED INVESTMENT IN DEPRECIABLE ASSETS; 1980, 1981, AND 1984, SELECTED INDUSTRIES**

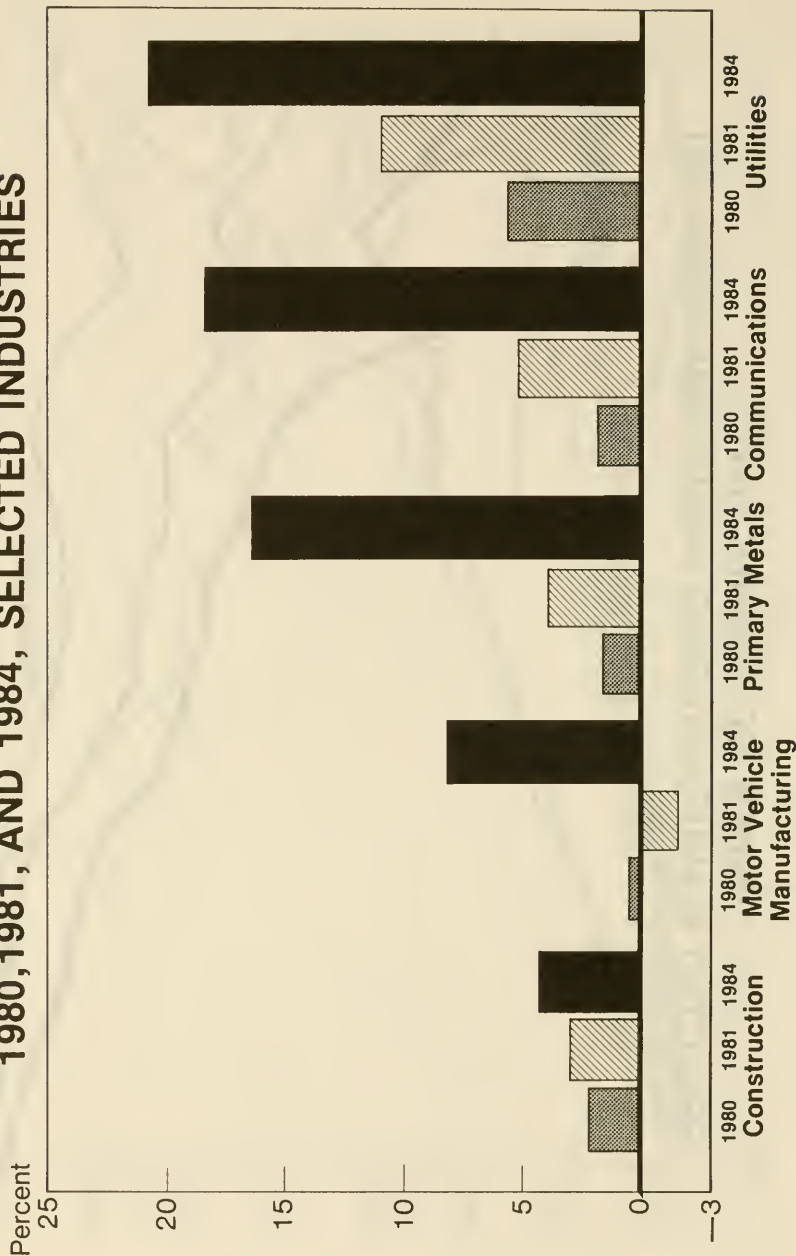
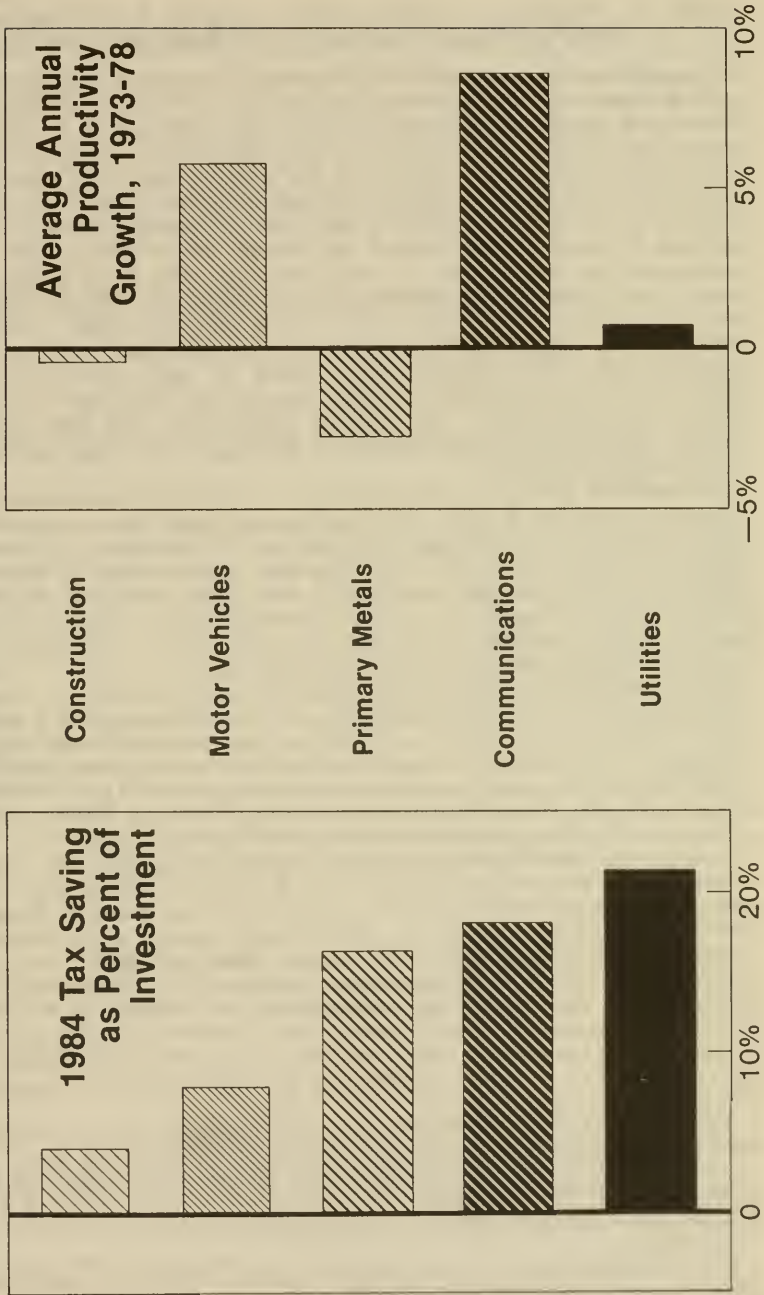




Chart 7  
**BENEFITS OF 10-5-3 AS COMPARED TO  
 RECENT GROWTH IN PRODUCTIVITY, SELECTED INDUSTRIES**



**Exhibit 47.—Statement of Secretary Miller, November 8, 1979, before the House Ways and Means committee, on a Federal value added tax**

It is a pleasure to appear before this Committee to discuss the important issues raised by H.R. 5665, the Tax Restructuring Act of 1979. This bill would result in fundamental changes in our Federal tax structure. Income taxes on corporations and individuals, as well as social security taxes, would be cut by \$130 billion in 1981. A Federal value added tax would offset this revenue loss. This testimony will not concentrate on the specifics of H.R. 5665, but on the basic issue which the bill raises: Whether the United States should replace some of its income taxes with a consumption tax; that is, whether the Federal tax system should weigh more heavily on consumption and less heavily on saving and investment. Many believe that such a change would contribute significantly to improved capital formation, higher productivity, and a more competitive position for American business in world markets. Others express concern that a consumption tax would have only small effects on investment and would place an unfair burden on lower income families already plagued by high prices for energy, food, housing, and other basic necessities of life. Higher consumption taxes, they believe, would mean still higher prices. These hearings will serve the valuable function of focusing the discussion on these significant economic and social issues.

An important element in this discussion is the role of a value added tax in the Federal tax structure. A value added tax is a multistage tax on consumer goods and services. Unlike a retail sales tax, it is collected at each stage in the production and distribution process. But since it is levied only on the amount of value added (the difference between sales and purchases) at each stage, rather than on the full selling price, it avoids the cascade, tax-on-tax, effects of a turnover sales tax. A value added tax is similar to a retail sales tax in that the total tax paid by the consumer is equal to the final price of the product multiplied by the tax rate.

Many European countries have value added taxes. Typically, they are imposed at a rate of about 15 to 20 percent and generate about 15 percent of a country's total national and local tax revenue. In contrast, state and local retail sales taxes raise about 7 percent of the total Federal, State, and local tax revenue in the United States. The \$130 billion in value added tax revenue estimated to be raised by H.R. 5665 would be about 14 percent of total Federal, State, and local 1981 tax liabilities, assuming it is accompanied by the proposed income and social security tax cuts.

In nearly all cases, the European value added taxes replaced sales taxes, frequently of the cascade turnover type which, unlike the value added tax, taxed the full sales price at each stage, without allowing a credit for tax on previous transactions. The Europeans found the cascade tax objectionable because it discriminated against nonintegrated firms and because the export rebate and import tax could not be accurately estimated for border adjustment purposes. Thus, in the European case, the adoption of a value added tax was regarded as a reform of an unwieldy and distortionary system of indirect taxation. This characterization does not apply to the present indirect tax system in the United States. Only the United Kingdom has used the value added tax to reduce income taxes, as Chairman Ullman is suggesting for the United States.

The popularity of the value added tax is not universal. The voters of Switzerland have twice rejected it by referendum. The latest rejection was based in part on a perceived threat to local autonomy since a Federal value added tax would have replaced some of the local Swiss taxes. Most recently, Japan, largely as a result of its parliamentary elections, appears to have postponed the planned introduction of a value added tax.

For the United States, a value added tax raises a number of important questions: Would it encourage capital formation? What impact would it have on the price level? Would it improve the trade balance? Would it be regressive? No one is seriously suggesting the value added tax solely as an additional Federal tax. Consequently, the answers to these questions, as well as others, depend upon which taxes the value added tax replaces. By way of illustration, two of the proposals made by Chairman Ullman call for reducing the corporate income tax and the social security taxes.

## Capital formation

Taxes on capital income such as the corporate income tax and the individual income tax on interest and dividends reduce the after-tax return on savings. Put another way, an income tax encourages present, as compared to future, consumption. With no taxes, a person with \$100 of income could choose between buying \$100 of consumption goods this year or saving now and buying \$110 of consumption goods next year, assuming the interest rate is 10 percent. Thus, a person can consume 10 percent more next year by saving now. Similarly, with a consumption tax, which exempts the earnings from capital, a person with \$100 of income could consume \$50 this year and pay \$50 in tax or, by saving the income this year, could consume \$55 next year and pay \$55 in tax. Thus, a person could still consume 10 percent more next year by saving now.

If a 50-percent income tax, rather than a consumption tax, is imposed, however, the individual, after paying the tax, can buy \$50 of consumption goods this year or can save the \$50 and, after paying the tax on the interest earnings, buy \$52.50 of consumption goods next year. Because of the income tax, a person can buy only 5 percent, rather than 10 percent, more consumption goods next year. Because of this lower return, the individual may decide to consume now rather than save for future consumption. It is important to recognize, however, that the responsiveness of saving to more favorable taxation is an unsettled issue. If one concludes that savings will rise in response to reduced taxation, then substituting a value added tax for the corporate income tax should encourage saving.

There are other considerations in assessing the mechanism that leads to an increase in investment. First, an increase in savings must be channeled into domestic financial markets in order to lower interest rates and therefore the cost of capital. Second, producers must respond to the lower cost of capital by using more capital intensive methods of production. There probably will be some response, but its magnitude is open to discussion. Third, the mix of new investment must be considered; it may be concentrated in housing, consumer durables, or fixed business capital. Thus, the substitution of a value added tax for the corporate income tax will increase capital formation only if savings increase, the cost of capital falls, and business responds by investing in the United States.

Finally, it bears noting that the potential of the value added tax for promoting capital formation may be exaggerated by an analysis that compares a "pure" consumption tax with a "pure" income tax levied on all returns to capital. The current income tax does not apply with full force to all types of saving and investment. For example, home ownership, pension reserves, and assets eligible for the investment tax credit or the asset depreciation range receive relatively favorable tax treatment. Similarly, not all forms of consumption would be taxed the same under any likely value added tax.

In contrast to an income tax, neither the social security tax nor a value added tax applies directly to the return from saving. Consequently, substituting a value added tax for the social security tax would be unlikely to affect savings decisions.

## Price level impact

A value added tax, by itself, will probably increase prices, since the tendency for business to pass the tax on to consumers is unlikely to be offset by an unduly restrictive monetary policy. The result would be a "one-shot" increase, not a recurrent increase, in the price level, although the subsequent price effects of adjustments in wage contracts, social security payments, and other indexed items may occur over time. In this regard, it is noteworthy that the Thatcher government's program of increased value added taxation and reduced individual income taxation has been accompanied by a significant increase in the consumer price index in the United Kingdom.

The important question, then, is whether the inflationary impact of the value added tax would be offset by reductions in other taxes. In the short run, the corporate income tax reduces the after-tax rate of return to capital, rather than increases product prices. Accordingly, prices will probably not fall as corporate income taxes are cut. Thus, substituting a value added tax for the corporate income tax is likely to increase prices. This is a serious drawback to the value added tax.



Substituting a value added tax for the social security tax may be less inflationary. Reducing the employer portion of the social security tax would tend to reduce business labor costs and possibly prices. Reducing the employee portion of the social security tax, however, would probably have no effect on the price level. Thus a value added tax, accompanied by an equivalent reduction in employer and employee social security taxes, would result in some increase in the price level. This would be particularly distressing to individuals least able to protect themselves from rising prices.

The impact of a value added tax on prices is largely independent of whether it is hidden in the price of the product or whether it is quoted separately to consumers. While it is not customary in Europe to quote the value added tax separately, this need not be the case in the United States. State retail sales taxes are quoted separately because the merchants persuaded legislators to require it, and the same could occur in the case of a United States value added tax. Furthermore, nonseparate quotation of the value added tax might be viewed as an attempt to hide the tax from public scrutiny.

### Balance of trade

Many have expressed the view that a value added tax would improve our trade balance. This is based on the observation that current international rules allow indirect taxes such as sales or value added taxes to be imposed on imports and rebated on exports. These adjustments are not allowed for direct taxes such as the corporate income or social security taxes. It is doubtful, however, that the U.S. trade balance would improve significantly from substituting a value added tax for the corporate income tax.

The impact of the value added tax on trade is closely related to what happens to prices. Quite simply, one must ask the question: Will the substitution of the value added tax for some other tax increase prices? It seems likely that the immediate impact of substituting a general value added tax of 5 percent for part of the corporate income tax would be to increase prices by about 5 percent. Since the new tax would be rebated on exports, just like our State retail sales and Federal excise taxes, exports would leave the country tax free. While domestic prices would be 5 percent higher, export prices would remain unchanged. Foreign consumers, therefore, would find U.S. products no more attractive than before; there would be no increase in demand for U.S. exports.

Since imports would be subject to the value added tax their prices also would increase by about 5 percent, the same as for domestic goods and services. As a consequence, domestic consumers would find imports just as attractive as before; there would be no incentive to reduce the demand for imports. Thus, on both the export and import side, there would be little immediate impact on the U.S. trade balance if a value added tax were substituted for the corporate income tax. There might, of course, be a positive trade impact in the long run if the substitution led to an improved investment climate, enhanced capital formation, and a more productive and competitive U.S. economy.

A modest trade balance improvement might result from replacing the social security tax with a value added tax, if the price level increased by less than the value added tax. Because of the price-dampening effect of reducing the employer portion of the social security tax, this is a possibility.

Regardless of which tax it replaces, many believe that a value added tax rebate, in itself, will expand exports and that a value added tax levy will retard imports. This belief might have a positive effect on trade if it encourages businesses to compete more vigorously in international markets. This result would depend upon the importance of nonprice considerations in explaining export activity.

It is also important to recognize that other countries could restructure their own tax systems if they felt the United States was gaining an unfair trade advantage. Relative to other countries, the United States has a moderately high corporate income tax, but a low social security tax. (See annex A.) Thus, the possibility exists that other countries might maintain their competitive position by increasing their existing value added taxes and reducing their corporate income or, especially, their social security taxes. This outcome is by no means certain. After all, a country's tax structure is not determined solely by international considerations. Moreover, except for Japan, U.S.

indirect taxes, as a share of gross domestic product, are the lowest of the major developed countries. (See chart 1 and annex A.) Other countries may believe that the United States should be allowed to 'tilt' its tax structure to reach some 'reasonable' or 'average' level of indirect taxation.

This issue has been studied before. Both the President's Task Force on Business Taxation, in its 1970 review of tax policy, and the Advisory Commission on Intergovernmental Relations, in its 1973 value added tax study, considered the trade issue. Both expressed doubt over any trade benefits resulting from substituting a value added tax for the corporate income tax and both noted the possibility of foreign retaliation.

### Distribution of tax burden

Lower income taxpayers, who must spend all their income on consumption, may find a value added tax burdensome because of its regressivity. While a value added tax, by itself, is regressive, one must consider which tax it replaces. The immediate impact of the corporate income tax is probably progressive since it falls on income from capital. Therefore, substituting a value added tax for the corporate income tax would make the tax structure less progressive. The social security tax, on the other hand, also is regressive because it is limited to the first \$22,900 of wages and applies only to labor income. Accordingly, substituting a value added tax for the social security tax would not make the tax system noticeably less progressive. One regressive tax would be substituted for another. Retired individuals, however, who do not pay social security tax, would be distressed by having to pay value added tax. They could justifiably say that they already had paid for their retirement during their working years and that higher prices and taxes in retirement were unfair. Their distress might be partially assuaged by the fact that social security payments are indexed.

One way to illustrate possible distributional effects is to ask what would happen to tax burdens if a value added tax completely replaced the individual income and social security (employee portion) taxes. (See chart 2.) The combination of the current income and social security taxes is progressive while a value added tax, even with necessities excluded, is regressive. As a share of income, the present individual income and social security taxes are only 2 percent for families with less than \$5,000 in income, but increase throughout the income range to 33 percent for families with over \$100,000 in income.

This may be contrasted with a value added tax with no exclusions at a 23.2-percent rate, sufficient to equal the revenue raised by the individual income and employee social security taxes in 1978. As a share of income, such a value added tax would be 35 percent for families with less than \$5,000 in income, but fall to 6 percent for families with over \$100,000 in income.

No one, of course, is proposing the complete substitution of the value added tax for the income and social security taxes. A more realistic alternative would be to substitute a value added tax for part of the combined individual income and social security taxes. One possibility would be to reduce income and employee social security taxes by \$100 billion, keeping the same degree of progressivity for these taxes as under present law, and offset the revenue loss with a \$100 billion value added tax with no exclusions. The resulting distribution of tax burdens would be regressive at the lowest income levels and mildly progressive elsewhere. As a share of income, families with less than \$5,000 in income would pay 17 percent in taxes, families with between \$5,000 and \$10,000 in income would pay 14 percent, and taxes would then increase throughout the income range so that families with over \$100,000 of income would pay 21 percent of their income in taxes. The overall distribution is significantly less progressive than the present combination of income and employee social security taxes.

The regressivity of the value added tax can be moderated, but not eliminated, by special measures. One possibility is the use of exemptions and reduced rates for necessities, as in Chairman Ullman's proposal and in some European countries. These reduce the tax burden of the value added tax at the lowest income levels, but the tax remains regressive. Exemptions and reduced rates, moreover, create administrative problems. A tax with two, three, or four rates is more complex than a tax with one

ANNEX A  
Federal, State and local tax revenues for selected countries as percent of gross domestic product, by type of tax, 1975  
[Country rankings in parentheses]

Country	Indirect taxes		Direct taxes							
	Total	Sales and excise <sup>a</sup>	Social security <sup>a,2</sup>			Corporate income	Noncorporate income <sup>3</sup>	Property <sup>4</sup>	Other <sup>5</sup>	Total <sup>6</sup>
			Total	Employer	Employee and self-employed					
Belgium .....	41.43(5)	10.87(6)	13.14(5)	8.44(4)	4.70(5)	3.07(6)	13.24(4)	1.01(12)	0.10(8)	30.56(4)
Canada .....	33.98(9)	10.94(4)	3.22(12)	n.a.	n.a.	4.67(2)	11.32(7)	3.13(3)	0.70(4)	23.04(11)
Denmark .....	43.05(4)	14.71(1)	48(13)	31(12)	17(12)	1.37(13)	23.86(1)	2.57(4)	0.06(10)	28.34(5)
France .....	36.90(6)	12.44(2)	14.72(3)	10.61(2)	4.11(6)	2.00(9)	4.58(13)	1.46(9)	1.70(2)	24.46(9)
Germany (Fed. Rep.) .....	35.22(8)	9.37(8)	12.03(6)	6.60(7)	5.43(4)	1.56(12)	10.60(8)	1.09(11)	0.57(6)	25.85(7)
Italy .....	32.34(10)	9.34(9)	14.83(2)	11.92(1)	2.91(9)	2.04(8)	4.95(12)	1.17(10)	0.01(11)	23.00(12)
Japan .....	20.23(13)	3.67(13)	5.09(11)	2.63(11)	2.46(10)	3.43(4)	5.07(11)	1.94(7)	1.03(3)	16.56(13)
Luxembourg .....	46.74(2)	9.72(7)	14.05(4)	7.80(6)	6.25(2)	7.22(1)	12.78(5)	2.34(5)	0.63(5)	37.02(1)
Netherlands .....	46.90(1)	10.91(5)	17.99(1)	8.40(5)	9.59(1)	3.61(3)	12.66(6)	1.48(8)	0.25(7)	35.99(2)
Sweden .....	45.96(3)	11.48(3)	8.89(7)	8.47(3)	0.42(11)	1.99(10)	21.17(2)	0.51(13)	1.92(1)	34.48(3)
Switzerland .....	29.49(12)	5.90(11)	8.49(8)	3.05(10)	5.44(3)	2.46(7)	10.51(9)	2.13(6)	-	23.59(10)
United Kingdom .....	36.77(7)	9.24(10)	6.71(10)	3.75(9)	2.96(8)	1.92(11)	14.29(3)	4.54(1)	0.07(9)	27.53(6)
United States .....	30.31(11)	5.49(12)	7.42(9)	4.18(8)	3.24(7)	3.29(5)	9.98(10)	4.13(2)	-	24.82(8)

Source: *Revenue Statistics of OECD Member Countries, 1965-75*.

n.a. Not available.

<sup>1</sup> Includes general sales, value added, and specific excise taxes.

<sup>2</sup> Includes contributions of employers, employees, and self-employed. Category is broadly defined to include all tax payments to institutions of general government providing social welfare benefits, provided they are levied as a function of pay or a fixed amount per person. Thus, for the United States this category includes contributions to the railroad retirement fund, unemployment insurance fund, workman's compensation fund, and civil service retirement program in addition, of course, to the more familiar social security-type payments made pursuant to the Federal Insurance Contributions Act (FICA).

<sup>3</sup> Includes income taxes on individual and unincorporated enterprises such as proprietorships and partnerships.

<sup>4</sup> Includes taxes on net wealth, immovable property, estates, and gifts.

<sup>5</sup> Includes taxes on employers based on payroll or manpower and miscellaneous taxes which cannot be classified within a specific direct tax category.

<sup>6</sup> Computed by subtracting sales and excises from total.



rate. The specially taxed items must be identified. Does a lower rate for food, for example, apply to such items as chewing gum, soda pop, candy, or caviar? Experience with the income tax shows that even medical services and drugs are not easy to define. Beyond the definitional problems, total or partial exclusions erode the value added tax base and its revenue potential. (See chart 3.)

The regressivity of a value added tax also can be reduced by a refundable income tax credit for tax paid on a necessary amount of consumption. This avoids the need to define exempt commodities and can be implemented at a lower revenue cost than a complete exemption for certain 'essential' commodities. It can, for example, be phased out at increased income levels. In effect, middle and upper-income groups would still pay tax on purchases of food and other necessary items. On the other hand, a refundable credit is effective only if it reaches the roughly 25 million individuals who do not appear on an income tax return. These tend to be individuals most in need of the credit, mainly recipients of social security benefits and of transfer payments under social and welfare programs. Unlike lower rates and exemptions, if the credit was not paid until the end of the year, the consumer would have to finance the tax during the year.

### Administrative and design considerations

Both the European value added taxes and the tax suggested by Chairman Ullman have certain basic similarities:

- They are broad based, applying to services as well as goods;
- Tax liability is determined by the credit method with tax paid on purchases deductible from tax due on sales;
- They are consumption type taxes, any tax paid on capital equipment purchases is immediately deductible; and
- They extend through the retail stage.

A value added tax of this type for the United States would involve about 15 million taxpayers. This number might be reduced by 5 million if exemptions were provided for very small proprietorships and farming. But under a value added tax, nearly all transactions are taxed. Even a firm that is tax exempt on its sales will have paid tax on its purchases. If it is to receive credit for tax paid on its purchases, it either would have to file a return or the credit would have to be made available to its customers.

Even 10 million taxpayers would add about 30 percent to the number of returns filed with the Internal Revenue Service, assuming quarterly returns are required. Since the value added tax would not totally replace any other tax and would be a new tax, requiring new returns, new regulations, and a new body of case law, this would be a net addition to the work of taxpayers, the Internal Revenue Service, and the courts. This differs sharply from the typical European case where the value added tax completely replaced another sales tax.

Reporting and payment requirements for a value added tax would be similar to those for Federal excises, which require liability to be computed on a semimonthly basis with payment due 9 days later. The actual excise tax return is filed quarterly and is accompanied by the payment of any remaining balance. Liquor and tobacco excises, however, have slightly different rules. A value added tax payment system which would fit more neatly with ordinary bookkeeping would be a monthly liability period with payment due at the end of the next month. This would be similar to that proposed by Chairman Ullman.

### Other considerations

A Federal value added tax would raise a number of other issues. Forty-five States and the District of Columbia impose general sales taxes, a revenue source which they tend to view as belonging exclusively to them. Sales and gross receipts taxes account for about 30 percent of State tax revenue. In contrast, excise taxes generate less than 4 percent of Federal tax collections. Nevertheless, while a Federal value added tax may make it more difficult for the States to raise their sales taxes, it should not prevent such increases. All levels of government, for example, impose income taxes. Moreover,

total Federal, State, and local sales tax collections are lower in the United States than in most developed countries.

Because of likely differences in the tax bases, it is doubtful that a Federal value added tax could be coordinated with the State sales taxes. Separate taxes, admittedly, would mean higher administrative and compliance costs. Each level of government would require a collection and audit capability. Taxpayers would have to become familiar with separate tax bases and separate returns. Revenue departments and taxpayers, however, already face this problem with Federal and State income taxes. Efforts aimed at Federal-State cooperation and coordination have not been successful.

As shown by Chairman Ullman's proposal, even a broad-based value added tax may not apply to all forms of final consumption. Practical considerations may require special treatment for many items. In the area of housing, for example, homeowners and tenants should be treated equally. But if rental payments are taxed, how should homeowners be taxed? It may be difficult to value the so-called imputed rent on owner-occupied housing. Taxing the purchase price of a home is one alternative, but this may aggravate the problems of many families already hard pressed to cope with high housing prices. The treatment of interest in the housing area also is troublesome. If it is exempt, what part of a rental payment should a landlord be allowed to exclude from the tax base? These and other problems will require careful study.

The value added tax is a very potent revenue source. At 1979 levels of consumption, a value added tax would raise roughly \$10 billion in revenue for each percentage point. Thus, a 7-percent value added tax would raise about as much revenue as the corporate income tax and a 12-percent value added tax would raise as much revenue as the social security taxes. With such a powerful instrument for raising revenue, many are concerned that the value added tax eventually will be used to add to the total Federal tax burden.

## Conclusion

Mr. Chairman, you are to be commended for initiating an examination of the very important, but complex, issues of how the Federal tax structure affects our national well-being. This is a time of great change. It is also a time of troublesome and unfamiliar economic conditions. The combination of high inflation, slow growth, and persistent trade deficits must make us wonder if the traditional economic remedies still work. In this sense, your decision to study a broad range of new initiatives could not come at a better time. But changes of such major consequences require careful and deliberate study. We welcome the opportunity to participate with you in that study.

Chart 1

# **DIRECT AND INDIRECT TAXES AS A PERCENT OF TOTAL TAX REVENUE**



# **TAX REVENUES AS A PERCENT OF GROSS DOMESTIC PRODUCT**

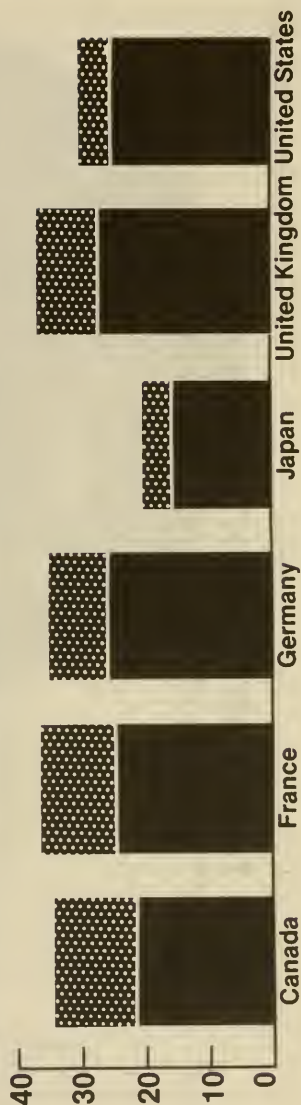




Chart 2  
**TAXES AS PERCENT OF INCOME**  
(Each line reflects equal total tax liabilities at 1978 levels of income)

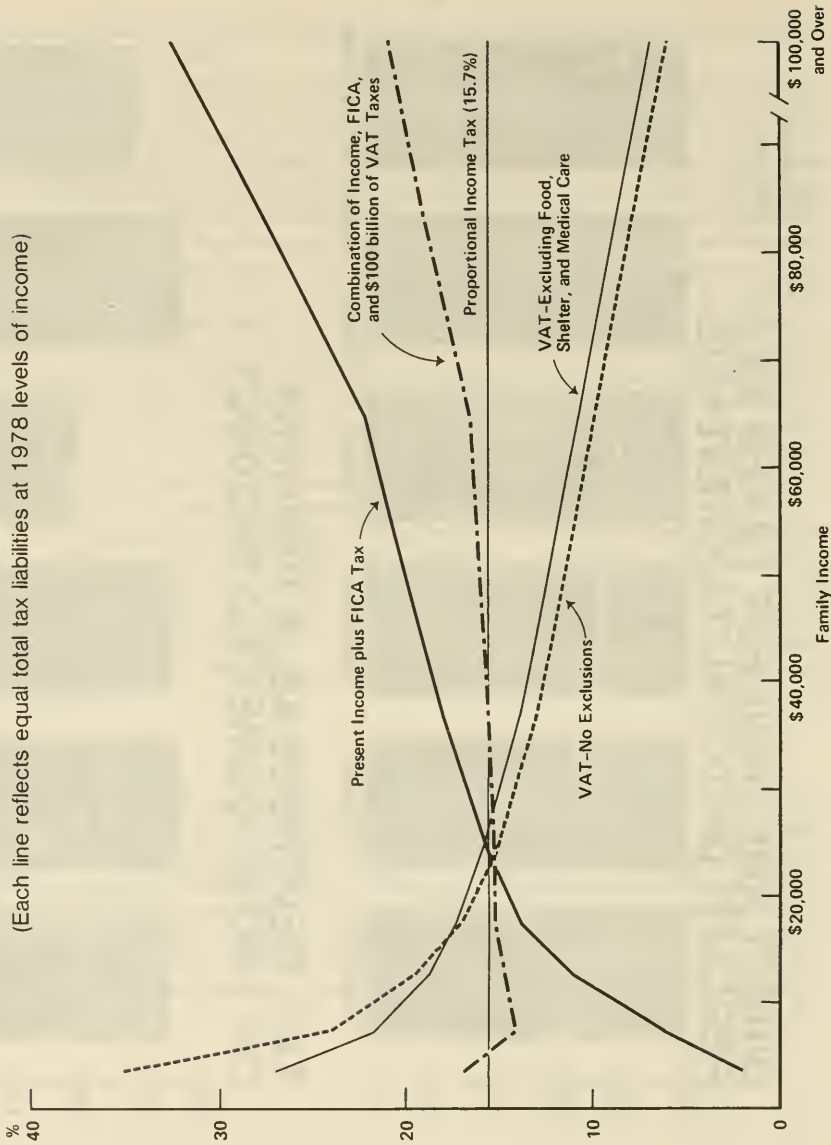
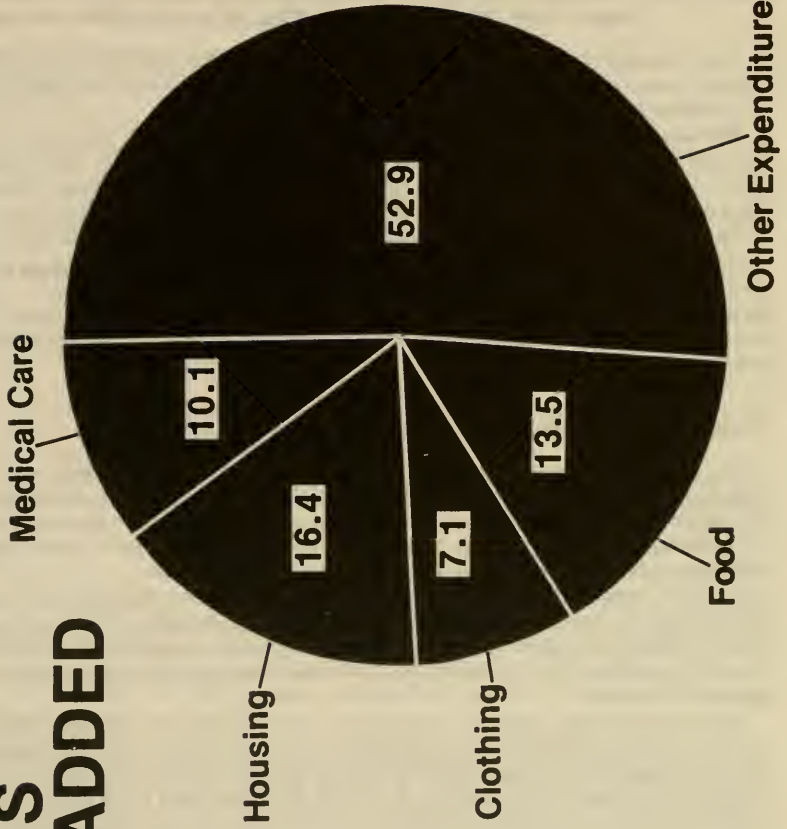


Chart 3

# SUBTRACTIONS FROM VALUE ADDED TAX BASE (Percent)



**Exhibit 48.—Statement of Assistant Secretary Lubick, January 29, 1980, before the House Ways and Means Committee, on tax incentives for saving**

I am pleased to be here today to discuss the general subject of tax incentives for saving, as well as to comment on specific proposals for savings incentives in which the Committee has expressed an interest.

Because of slower growth in the economy this past decade, there have been increasing calls for a tax system more focused on consumption than income or one more focused on wages than on income from investment. However, despite recent expressions of concern, the debate is not new, and policymakers often have responded in the past by enactment of tax provisions which directly or indirectly reduce the taxation of income from assets. Many reductions have been enacted in recent years, including a lower rate of taxation on capital gains, expansion in types of tax-exempt State and local bonds, increased options for pension savings, investment tax credits, accelerated depreciation, and decreases in rates of tax applying to high-income taxpayers.

**Existing tax expenditures for individual saving and investment**

My testimony today will be confined to tax incentives for saving and investment which apply primarily to individuals or which are reflected on individual tax returns. Nonetheless, it must be recognized that the split between individual and business tax incentives is arbitrary; since businesses are owned by individuals, business tax incentives affect individual decisions to invest and save.

Table 1 summarizes the existing tax expenditures for saving and investment by individuals. Because of the interaction among the provisions, one must be cautious in simply adding together the various tax expenditures. Nonetheless, if all tax expenditures for individual saving and investment were eliminated, tax receipts would rise by about \$70 billion.

One can compare these tax expenditures to the actual tax receipts from individual income taxation of income from capital. If one were to subject only wage income to the individual income tax, while excluding all income from capital and disallowing interest deductions, the reduction in liabilities would have been about \$35 billion for calendar 1979. [This example assumes that capital income includes one-third of sole proprietorship and partnership income, one-half of pension income, and nine-tenths of royalty income. Different plausible estimates of the ratio of capital to labor income from these sources of income do not significantly change the estimate of individual income taxes collected on capital income.] Even allowing an interest deduction, while excluding all capital income from taxation, would reduce liabilities only by \$51 billion. In summary, *individual income tax expenditures for income from capital are considerably in excess of individual tax collections on income from capital.*

TABLE 1.—*Tax expenditures for saving and investment by individuals, fiscal 1981*  
[ \$ millions. Excludes corporate tax expenditures ]

Description	Amount
<i>Expenditures primarily related to financial and nonbusiness tangible assets of individuals:</i>	
Exclusion of interest on State and local debt .....	3,865
Nonrealization of capital gains at death .....	5,085
Sixty percent exclusion of long-term capital gains .....	14,885
Dividend exclusion .....	515
Capital gains exclusion and tax-free rollover of personal residences .....	1,700
Deductibility of interest on home mortgages and consumer credit .....	19,000
Exclusion of pension contributions and earnings .....	17,260
Exclusion of interest on life insurance earnings .....	3,895
Deferral of interest on U.S. savings bonds .....	250



*Expenditures related primarily to noncorporate  
business assets held by individuals:*

Capital gains treatment for agriculture, timber, coal, and iron ore .....	640
Special provisions for depreciation and rapid amortization .....	755
Investment credit .....	3,180
Expensing of capital outlays: Agriculture, construction, research, exploration, and development .....	1,425
Excess of percentage over cost depletion .....	1,670
Tax incentives for preservation of historic structures .....	45
Total, disregarding interaction .....	74,170

### Assets and liabilities of individuals

Perhaps an easy means to see why so much income from capital is not subject to the individual income tax is to examine in more depth the portfolio of assets and liabilities held by individuals in the United States. In the tax expenditure budget, the largest individual tax expenditures for capital income relate to housing, pensions, life insurance, and capital gains on the sale of land, business assets, and corporate stock. Correspondingly, if the portfolios of individuals are examined, it is found that most of their savings resides in the exact same assets.

Of some \$8 trillion in assets held by individuals, \$4.5 trillion are in tangible assets such as housing, durables, and land. Benefits provided by owner-occupied residential housing and durables are not subject to tax (although interest payments on mortgages and installment debt are deductible, as are property taxes). Neither is income from investment real estate taxed fully, as owners of these assets are allowed to depreciate what often are appreciating assets. Very little capital gains tax is collected on land, not only because of capital gains rates, but, more importantly, because increases in value of land are deferred from taxation until realized—which is often never. Much of the remaining income from land and buildings avoids taxation, as can be evidenced by the low amounts of rental and farm income reported on tax returns relative to national income estimates of income received.

Individuals also hold \$3.5 trillion in financial assets. Over 20 percent of that total, or \$729 billion, now resides in life insurance and pension reserves. Earnings on savings in life insurance and annuities are usually deferred, often permanently, from taxation. The current tax treatment of an individual's retirement savings in a qualified plan is equivalent to complete exemption of the earnings on that savings if the taxpayer is in the same tax bracket when he receives his pension as when his employer (or, in the case of an IRA or Keogh plan, the individual) deposits money in a pension plan. If the taxpayer is in a lower tax bracket, as is usually the case, the tax treatment is equivalent to a subsidy for deferred wages in addition to nontaxation of the income from savings.

Another \$809 billion of the financial assets of individuals are held directly in corporate stock. In the individual income tax, corporate stock is given favorable tax treatment through the exclusion of 60 percent of gains from taxation, the dividend exclusion, and, most importantly, the deferral of taxation of any gains until realized, if at all.

Finally, individuals hold \$75 billion worth of State and local obligations, the income from which is nontaxable, and \$81 billion worth of U.S. savings bonds, the income from which is usually taxed only when the bonds are redeemed. Demand deposits and currency, of course, are not taxed because they do not yield any interest income.

*Of the \$8 trillion in individual assets, then, less than 20 percent is in a form for which there is not some direct tax expenditure through deferral, capital gains rates, exclusions, or other means of nontaxation of the income from the asset.*

TABLE 2.—*Assets and liabilities of individuals in the United States—1978*  
[\$ billion. Yearend outstandings]

Tangible assets .....	4,514
Reproducible assets .....	3,230
Owner-occupied housing .....	1,448
Other residential structures .....	395

Consumer durables .....	793	
Inventories and nonresidential plant and equipment .....	594	
Land .....	<u>1,283</u>	
Residential .....	517	
Nonresidential .....	567	
Vacant .....	200	
Total financial assets .....		3,491
Currency, savings accounts, and money market funds .....	<u>1,349</u>	
Demand deposits and currency .....	242	
Time and savings accounts .....	1,096	
Money market fund shares .....	11	
Securities .....	<u>1,188</u>	
U.S. savings bonds .....	81	
Other U.S. Government securities .....	123	
State and local obligations .....	75	
Corporate and foreign bonds .....	65	
Open-market paper .....	36	
Corporate equities .....	809	
Pension and life insurance reserves .....	<u>729</u>	
Private life insurance reserves .....	190	
Private insured pension reserves .....	119	
Private noninsured pension reserves .....	199	
Government insurance and pension reserves .....	221	
Miscellaneous assets .....	<u>225</u>	
Total assets .....		<u>8,004</u>
Total liabilities .....		<u>1,503</u>
Mortgages, owner-occupied nonfarm homes .....	738	
Consumer credit .....	340	
Non-corporate business mortgage debt .....	213	
Security credit and policy loans .....	53	
Other debt .....	159	
Net worth .....		6,501

Source: *Balance Sheets of the U.S. Economy*. (Washington: Board of Governors of the Federal Reserve System, 1979).

### The deduction for interest paid

Before turning to specific proposals for incentives for saving, the tax deduction for interest paid must be examined more closely. As long as it is possible for individuals to deduct all interest payments currently, while at the same time receiving a tax subsidy for certain types of investment, the incentive effect of any subsidy will be reduced substantially. Imagine a simple case in which a taxpayer can borrow or invest in a given asset at a 10-percent rate. Suppose the income from the asset is subsidized through a partial exclusion, credit, or deferral of taxation so that the taxpayer need only include 5 percent of the 10-percent rate of return in income subject to tax. However, he is allowed to deduct immediately all interest paid on borrowings. The taxpayer then has an incentive to invest in the asset, but not necessarily to save. For instance, if the taxpayer is in the 50-percent tax bracket, by borrowing \$10,000 and investing it in the subsidized asset, his net savings equals zero, yet his tax subsidy equals \$250. If he saves \$10,000 and invests it in the asset, his tax subsidy still only

equals \$250. Thus, the tax preference provides him no additional return for increasing his net savings.

	<i>Borrower</i>	<i>Saver</i>
A. Earnings on asset .....	\$1,000	\$1,000
B. Interest paid .....	1,000	0
C. Change in taxable income before exclusion (A-B) .....	0	1,000
D. Exclusion or other tax preference .....	500	500
E. Change in taxable income after exclusion (C-D) .....	-500	500
F. Tax savings (= (C-E) $\times$ .5) .....	250	250

The law does place some limits on investment deductions in excess of investment receipts, but, since money is fungible, these limitations can be avoided easily by borrowing on assets such as housing or assets used in business or by increasing consumer debt.

Contrary to expectations, what is thought to be incentive to invest may actually become a disincentive to work and save. This arises for two reasons. First, the person who can generate such tax savings without doing any additional saving or productive labor may begin to devote more and more time to such nonproductive efforts. The tax savings itself reduces the need to work or save in order to generate income. Equally as important, the revenues lost to taxpayers who do not increase their savings usually must be collected from other taxpayers. These taxpayers face higher tax rates on their wages and on their income from capital. The net increase or decrease in total savings is uncertain.

These economic effects should not be viewed as minor or inconsequential. It is quite common for individuals to borrow at the same time that they invest in subsidized investments such as pensions, annuities, land, or corporate stock. These individuals receive the same tax subsidy as those who increase their net savings when they invest in these assets.

### Implications for further saving incentive proposals

The existing plethora of savings and investment provisions in the individual income tax have been adopted over time in piecemeal fashion. There is no established relationship among these various provisions, nor is there consistent treatment of income from various forms of capital. The ability of taxpayers to switch their assets from one form to another, or to borrow in order to invest in a tax-preferred asset, has mitigated if not eliminated the ability of many of these provisions to increase overall savings. For the economy as a whole there has resulted inefficiency in the allocation of resources and increases in the price of many assets. Revenues lost because of tax preferences for certain types of income are offset by increases in rates of taxation on income from other assets and from work. In summary, we have proceeded far from a tax system in which all income is subject to tax, but without any basic direction as to where we are going. At some point we must pause and ask ourselves whether continuing to proceed in such a piecemeal fashion will reduce or increase the inequities and inefficiencies of the current system.

### Specific proposals

With this background in mind, let us now turn to some specific types of proposals for tax incentives for saving. We will deal with four categories of saving incentives: (1) Exclusions and credits for interest and dividends; (2) deferral of tax for deposits and earnings on deposits in special savings accounts or trusts; (3) nontaxation as ordinary income of dividends reinvested through a dividend reinvestment plan; and (4) modifications to the tax treatment of individual retirement accounts.

*Exclusion and credits for interest and dividends.*—A number of bills have been introduced in Congress recently to exclude from taxation a portion of interest or interest and dividends. A few proposals provide a credit against tax for a percentage of such income received. On December 17, 1979, the Senate voted to provide for an



exclusion of up to \$201 for singles, or \$400 for married persons filing jointly, for interest and dividends received.

The Treasury opposes these proposals. We believe that the proposals are expensive, they do not stimulate savings effectively, and they do not deal adequately with the issue of tax-deductible borrowing for the purpose of securing a tax-free return. These proposals are little more than a complicated way of providing middle-income tax relief. [We do, however, favor the extension of any exclusion or credit to include dividends as well as interest. This lessens the extent to which the taxpayer can obtain the tax subsidy merely by shifting the form of his savings, and it results in some simplification of the Code, since the existing dividend exclusion is folded into the new provision.]

The revenue loss from these proposals is quite large relative to the amount of savings they stimulate. While costing about \$2 billion annually, for instance, the Senate bill would not stimulate savings effectively because, for the most part, it does not operate on the margin of decisionmaking. At the margin no incentive effect whatever is provided to savers who earn more than \$400 of interest and dividends. Currently, such savers earn over 95 percent of all interest and dividends. While the Senate bill provides no incentive effect to these large savers, they, nonetheless, are eligible for the full \$400 exclusion and would receive three-quarters of the total tax break resulting from the bill. Thus, three-quarters of revenue loss (or about \$1.5 billion) would go to the largest savers and would do little to encourage saving.

Some marginal incentive to increase saving would be provided to the small savers with less than \$400 of interest income, a group which now contributes a small share of aggregate savings. Even in the unlikely event of a substantial increase in the savings of this group, however, aggregate savings in the economy would be little affected. [The Senate bill would raise the average after-tax return of savers with less than \$400 of interest income by no more than one-third. Even under the assumption of an extremely high savings response to an increase in after-tax return (assume an interest elasticity of 0.4), such small savers would increase their holdings of interest-earning assets by no more than 12 to 13 percent. This, in turn, would represent an increase of only 1 percent in holdings of all interest-earning assets or less than one-quarter of 1 percent in holdings of all assets yielding capital income. Moreover, since taxpayers can borrow to obtain the tax subsidy, even these estimates must be considered high. Thus, the increase in aggregate savings would be imperceptible.]

We agree that small savers are now treated unfairly; they generally receive a very low return on savings accounts, a return that is less than the current rate of inflation. Moreover, small savers are ordinarily unable to take advantage of higher yielding alternatives such as money market certificates because of minimum deposit requirements. While interest and dividend exclusions would provide some relief to small savers, the simplest and most effective way to provide assistance is to phase out Regulation Q, which is what forces small savers to accept an unfairly low return.

This can be illustrated by a hypothetical example. Consider a saver in the 21-percent bracket (e.g., a family of four making \$18,000 a year). For the purpose of this example we will assume that this saver might earn 9 percent before taxes and 7.2 percent after taxes on passbook savings once Regulation Q is phased out. However, the maximum amount now allowed on passbook accounts under Regulation Q is 5.5 percent. Even if the entire 5.5 percent is tax-free, the small saver in our example is 1.7 percentage points better off if Regulation Q is phased out than if the Senate bill is enacted.

Equally as important, the phaseout of Regulation Q allows an increased incentive to apply to all savings; i.e., there is no cap on the amount of interest eligible for the higher rate of return. Thus, we believe that support for the phaseout of regulation Q is a much better means of helping the small saver and, at the same time, providing a savings incentive for the economy as a whole.

Finally, the Senate bill, like most proposals for exclusions or credits, fails to deal with the issue of tax-deductible borrowing for the purpose of obtaining tax-free income. Any proposal designed to subsidize interest income should limit the potential for "gaming" the tax system by simultaneous borrowing and lending transactions. By not requiring interest income to be netted by interest deductions, the proposal grants benefits to individuals who need not change their savings behavior.

*Deferral of tax on earnings from savings accounts or trusts.*—Another type of “savings incentive” proposal would grant tax breaks to taxpayers who deposit money in special savings accounts or trusts. The tax subsidy results from deferral of tax on all earnings on the deposits. Additionally, deductions are sometimes allowed for deposits made; when withdrawn, these deposits may be taxable or may simply reduce the basis of purchased assets. In some proposals, withdrawals from accounts are required to be spent on housing (individual housing accounts) or education (individual education accounts); in other proposals, the tax subsidy is intended merely to encourage savings, and it does not matter for what purpose the savings is spent. Most proposals limit the amount of deposits eligible for the tax break.

There are a number of difficulties with these proposals. They clearly violate principles of tax law that all individuals with equal incomes should pay equal tax and that all income should be equally subject to tax. In part, the violation of these principles is accepted by proponents of the proposals because they are trying to move the base for the income tax away from income and toward consumption.

Despite the intention, however, it is quite difficult to move “part way” toward a consumption tax by providing special tax subsidies in the income tax. Perhaps the greatest difficulties arise when the treatment of borrowing is ignored and the subsidy is limited to certain types and certain amounts of savings.

In the case of existing proposals, they all suffer from the defect that the tax savings do not depend upon an increase in household savings. The taxpayer needs merely to borrow whatever money is necessary to deposit in the special savings account. In such cases the tax system cannot only be “gamed”, but, in effect, tax rates are raised and the tax disincentives created for taxpayers who do not “game” the system. Moreover, since the incentive only applies to certain savings, it primarily causes taxpayers to reallocate the assets within their portfolios rather than increase their total savings. With a cap on the amount of savings eligible for the tax break, the savings incentive is made even weaker, since many taxpayers will be given no savings incentive whatsoever if they already have savings in excess of the amount necessary to receive the maximum tax break.

There are some additional difficulties as well. The incentive to reallocate savings toward tax-preferred accounts may result in a misallocation of resources in the economy. For instance, earnings from sheltered savings accounts or trusts may discourage direct investment in business if those earnings are not similarly sheltered. In the case of education and housing accounts, penalties are assessed against the taxpayer for spending savings on nonapproved items. Besides the difficult administrative problems that such a provision causes, it also locks people into certain types of consumption and penalizes them for changing their mind. In some cases, a taxpayer could be penalized because he withdraws money to cover hospital or other emergency expenses. Even when the form of consumption is not limited, it should be realized that the tax is most likely to be paid when persons need the money the most, that is, when they withdraw it from the accounts.

Finally, we would expect that the distributional effect of these types of proposals would be quite regressive. Exclusions, deductions, and deferrals are worth the most to taxpayers in the highest income brackets. For nontaxable persons, there is no subsidy at all. Some of these proposals are in part modeled on IRA accounts. As I will indicate later, the distribution of benefits from these accounts primarily goes to upper income individuals, and only a small percentage of low- and middle-income taxpayers eligible to use these accounts actually use them.

*Dividend reinvestment plans.*—Treasury opposes proposals to allow deferral of taxation on dividends reinvested in stock through dividend reinvestment plans. Under one bill, H.R. 654, up to \$1,500 (\$3,000 on a joint return) of dividends would be tax exempt if reinvested in a qualified dividend reinvestment plan. Under such a qualified plan, a corporation would issue new shares of common stock to shareholders who elect to participate. The new stock would be issued at fair market value or at a discount not to exceed 5 percent. Shareholders who elect not to participate would continue to pay tax on cash dividends received.

Special tax rules would apply to stock purchased under a qualified dividend reinvestment plan. If such stock is sold within a year after issue, the entire amount



received would be treated as ordinary income. If the stock is held for more than a year, this amount would be taxed as a long-term capital gain.

The effect of this bill would be to give shareholders an option to convert cash dividends into earnings retained on their behalf. These optional retained earnings would generally be taxed in a manner similar to actual retained earnings; they would not be included in the shareholders' income but would be taxed as capital gains if the shareholder sells his stock.

Under current law, investors can seek the optimal mix of cash flow and retained earnings from stocks by choosing the type of stock that suits their needs. Investors in high tax brackets who seek to defer tax on retained earnings can buy stocks with low dividend/earnings ratios; investors in low tax brackets who are interested in cash flow can buy stocks with high dividend/earnings ratios.

This bill enables shareholders to realize the tax benefits of retained earnings without purchasing growth stocks. Consequently, the effect of this bill would be highly regressive. The major beneficiaries would be high-bracket investors who could obtain the benefits of deferral without assuming the risks generally associated with growth stocks. Low-bracket investors and retired people would not benefit because they would generally choose to receive cash dividends.

In addition, tax-motivated borrowing would be encouraged to the extent it is easier and less risky to borrow against stock in a secure, high-yield company. For example, a wealthy investor who borrows on margin to purchase shares of a public utility would be able to receive a tax-free accumulation while deducting interest paid on the margin account. Because investors can also reallocate their portfolios to receive this tax break, they need not increase their savings in order to receive the benefits of the bill.

A dividend reinvestment proposal resembles past proposals to relieve double taxation of dividends only to the extent it provides a tax break for shareholders. However, other effects are exactly the opposite of double tax relief as ordinarily understood. Rather than encouraging a more flexible capital market, as do other proposals for double tax relief, it encourages retention of earnings within each corporation. Rather than providing that dividends are taxed once at the marginal rate appropriate to each shareholder, it taxes them at corporate rates.

The revenue loss from H.R. 654 would be \$640 million in calendar year 1980 and slightly over \$1 billion in calendar year 1984. However, the longrun cost could be significantly more, since the bill's ultimate effect is to allow shareholders to have their dividends taxed at capital gains rates, if taxed at all.

*Individual retirement accounts.*—Changes in the law relating to tax-favored retirement savings have often been proposed as savings incentives. However, other issues of pension and retirement policy are also involved in proposals relating to tax-favored retirement savings and we would like to discuss some of our concerns in this area.

As we have previously testified, [Statement of Daniel I. Halperin, Deputy Assistant Secretary (Tax Legislation) on April 3, 1979 before the Senate Finance Committee Subcommittee on private pension plans and employee fringe benefits] we support the objective of broadening retirement savings. However, we feel it is essential that any proposal to increase retirement savings assure adequate, nondiscriminatory coverage and benefits. The enjoyment of tax benefits associated with savings for retirement must be widespread. It is not enough that benefits be generally available; broad-based utilization must also be present.

Tax incentives for retirement savings are justified as a means of assuring that employees at all levels of compensation will be provided with retirement protection. However, without a requirement that favorable tax treatment for retirement savings be utilized by persons at all income levels, the tax system will prove to be a poor means of providing for the retirement of those with low or moderate incomes. The higher a taxpayer's income, the greater the benefits of a deduction. Thus, in absence of a requirement for coverage of employees at all income levels, tax benefits and, ultimately, retirement security will accrue only to those who are given the greatest incentive to save in pension plans. This result is dramatically illustrated by recent figures on deductions for contributions to individual retirement accounts, annuities, and bonds (IRA's). Employees who are not active participants in employer-sponsored plans are eligible to make deposits in IRA's. Yet, in 1977, while over 52 percent of



eligible employees with adjusted gross income of \$50,000 or more utilized IRA's, the average utilization rate was under 5 percent for those with \$20,000 or less (Table 3).

Many proposals expand the IRA concept by allowing deductions for contributions by active participants. We are concerned with the distributional consequences of tax incentive programs which allow deductions and are modeled on existing IRA provisions. We note that a different approach has been proposed by Mr. Gibbons in H.R. 5693. Under H.R. 5693, a tax credit equal to 25 percent of an employee's contributions for a year would be allowed for both individuals who do not participate in a plan and individuals who are active participants in an employer-sponsored plan. The maximum annual employee contribution taken into account for purposes of the credit would be the lesser of \$1,500 or 15 percent of compensation, the limit applied to IRA's now. It is possible that the tax credit approach reflected in H.R. 5693 will satisfy some of our concern regarding discrimination since the tax benefit associated with the credit is more attractive to lower income individuals and will not be as attractive to those at higher income levels. Thus, the need for specific antidiscrimination rules may be reduced. However, care must be taken to assure that there will be widespread participation at all income levels.

We understand the Committee's concern in this area. We are interested in pursuing the proposals which have been made and will be pleased to work with your staff on these matters.

TABLE 3.—*Individual retirement accounts, 1977: Estimate of utilization rate by income class*

Adjusted gross income class	Number of returns with salaries and wages <sup>1</sup>	Estimated number of taxpayers with salaries and wages <sup>2</sup>	Estimated number of taxpayers eligible to use IRA's <sup>3</sup>	Estimated number of IRA's <sup>4</sup>	Utilization rate
		<i>Millions</i>			<i>Percent</i>
0-\$5,000.....	20.1	20.7	17.6	0.04	0.2
\$5,000-\$10,000.....	16.5	19.0	13.3	.18	1.4
\$10,000-\$15,000.....	13.0	17.5	10.5	.35	3.3
\$15,000-\$20,000.....	10.7	16.3	7.4	.40	5.4
\$20,000-\$50,000.....	15.8	24.9	6.2	1.35	21.8
\$50,000 and over.....	1.1	1.4	.4	0.21	52.5
Total.....	77.2	99.8	55.4	2.53	4.6

<sup>1</sup> Unpublished data from 1977 tax returns.

<sup>2</sup> Includes two spouses when both have salaries and wages.

<sup>3</sup> Excludes persons covered by public or private retirement systems.

<sup>4</sup> Allows for two individual retirement accounts on some returns.

Based on number of forms 5329 filed. Some of these accounts reported no deductible contributions during 1977.

## Summary

In summary, there are numerous tax expenditures in the Code which favor individual savings and investment. Most household savings is actually in assets for which there is some tax break allowed for the income from those assets. Since there are about \$70 billion of tax expenditures for individual savings and investment, we should not be led to believe that an expenditure of a few billion more dollars would result in any major change in the rate of return on savings or the amount of savings in the economy. We also need to recognize that almost all proposals for individual saving incentives violate the principle of the tax law that all income should be equally subject to tax. A vote to subsidize a certain type of saving is simultaneously a vote to increase the relative taxes on earnings from nonsubsidized savings and from work.

Specific proposals need to be examined closely to see if they do result in additional incentives to save; these incentives, if they exist, must then be compared to the disincentives created by the increase in the relative rate of tax on other income. Proposals should not allow taxpayer to "game" the tax system merely by shifting the

form of their savings, nor to gain a tax subsidy on interest and dividends received if, at the same time, all interest expense is deductible. Retirement savings proposals should be designed to result in increased retirement savings in the economy and increased retirement income for individuals at all income levels.

Budgetary considerations do not permit new tax initiatives at this time. However, as the President has stated, "when tax reductions are timely, they should be designed to achieve multiple objectives—not only reducing the tax burden and stimulating growth, but raising investment and productivity and reducing inflation, as well." Therefore, when appropriate, we would like to examine with you various options for tax reductions, including possible incentives for savings and investment. Choices among all approaches would then be based on considerations of equity and relative effectiveness in meeting each of the objectives outlined by the President.

**Exhibit 49.—Statement of International Tax Counsel Rosenbloom, April 29, 1980, before the Subcommittee on Oversight of the House Ways and Means Committee, on the tax treaty policy of the United States**

Thank you for inviting me to participate in a panel discussion today. I am grateful for this opportunity to discuss U.S. policy regarding tax treaties.

The questions raised in your letter inviting my testimony included: What the tax treaty policy of the United States is; what it should be; how that policy is formulated; and whether the policy should be different for developing, developed, and tax haven countries. In addition, you asked me to comment on a number of specific aspects of the process of formulating and implementing tax treaty policy.

These questions are very far reaching.

Tax treaties represent a highly developed area of international cooperation. Few fields come to mind in which international groups have worked so consistently for so long. The model treaties produced through these efforts by, for example, the Organization for Economic Cooperation and Development constitute major achievements. Indeed, one is tempted to address your questions by referring only to the treaty materials that exist today, including the U.S. model treaties, and to review outstanding policy issues simply by comparing models and discussing their differences.

The existing models do not, however, speak to the question of what tax treaty policy might be. Because they reflect more than a half century of experience among nations, the models tend to assume answers to some fundamental questions.

These fundamental questions are: What is the purpose of tax treaties? Are bilateral treaties the optimum means of carrying out those purposes? Is the basic approach employed by existing models the best form of bilateral agreement?

A serious review of U.S. tax treaty policy must begin with these questions. For this reason, the first part of my statement describes the history of international efforts to achieve "tax harmonization." This part ends with a summary of the highlights of the OECD model income tax treaty, which forms the essential basis of current U.S. tax treaty policy.

The second part of my testimony focuses upon the U.S. experience: Our treaties currently in force; the present U.S. model income tax treaty and its differences from the OECD model; and the major "collateral" issues which are of significance in current negotiations. Because most of the Subcommittee's questions relate primarily to income tax treaties, I will not discuss estate and gift tax treaties. I note, however, that significant activities are underway with respect to such treaties.

In concluding, I will discuss the overall "management" of the tax treaty program: The process of designing and modifying the U.S. model; how countries are selected to negotiate with; the 'bargaining' process involved in treaty negotiations; the implementation of a treaty once it enters into force; and the degree of public participation in the treaty process.

## I. International Efforts to Achieve Tax Harmonization

### A. The antecedents

What we now call "direct" taxes—taxes imposed directly on income or property—did not come into widespread use until the late 18th and early 19th centuries. From the first, states imposed such taxes on a dual basis, sometimes taxing because of a relationship to the person (for example, because he was a resident of the state), sometimes taxing because of a relationship to the property or income (for example, because the property was located in the state's territory). This dual basis of taxation obviously created a potential for two states to claim a right to impose the same kind of tax on the same base. But in early times this did not generally pose a practical problem because international commerce was not highly developed and tax rates were relatively modest.

Double taxation was, however, a problem for states that were closely related by language, history, or custom, and for political subdivisions of the same state. Quite frequently in these situations, important commercial relations were threatened by direct taxes imposed on a dual basis. These situations thus gave rise to the earliest forms of "tax harmonization" laws, and interstate or international tax agreements, particularly among the Germanic states of Central Europe in the late nineteenth and early twentieth centuries.

During and shortly after World War I, double taxation became a matter of worldwide significance. Rates of direct taxation, particularly income taxation, were increasing, as was the volume of international business. In the United States, this led to the enactment, in the Revenue Act of 1918, of provisions embodying a "foreign tax credit," which allowed a deduction from the U.S. income tax of the lower of the amount paid to a foreign government as an income tax or the U.S. tax attributable to a taxpayer's foreign income. In 1920, a conference of representatives of most members of the League of Nations recommended to the League's Financial Committee that it study international double taxation and recommend means of alleviating it.

In a 1923 report commissioned by the League, four economists, from the United States, the United Kingdom, the Netherlands, and Italy, discussed the economic consequences of international double taxation; the principles governing the competence of states to impose taxes on "international" property or income; and the application of those principles in developing technical means of eliminating double taxation. For the first point—economic consequences—the economists used the model of a tax imposed in an "origin" or source country which supplements a preexisting tax imposed by the country of the investor's "residence." They concluded that the principal consequence of such a tax for preexisting investments was a diminution of the value of the investment, and thus a penalty on the foreign investor. With respect to new investments, the tax was not a "burden" on the investor, since it would be discounted in making the investment and the investor could, if necessary, forego the investment altogether. Rather, the "penalty" was ultimately on the source state itself, or its consumers; the tax would raise the rate of return that an investor would demand before investing in that state. The "double" tax was, in effect, a protective tariff on the import of capital into the source state.

In regard to international competence to tax, the economists described two broad principles of modern direct taxation: "ability to pay" and "economic allegiance." The first point was simply that taxpayers should bear their share of the burden of government revenue needs in proportion to their ability to pay. The problem posed by this concept in an international context was identifying the group of persons whose "ability to pay" should be taken into account in allocating tax burdens. The economists concluded that this group should comprise those persons who owed the taxing power "economic allegiance" with respect to the property or income being taxed.

Four "elements" of economic allegiance were identified: where wealth originated; where wealth, once produced, was kept; where laws created or protected enforceable rights to wealth; and where wealth was consumed, disposed of, or enjoyed. The economists then discussed the implications of "economic allegiance" for the rights of states to tax different categories of wealth or income.



- With respect to wealth derived from *land*, the state where the land was located was the dominant factor in production; the land, of course, remained in the source state; that state's laws ordinarily protected rights to land; therefore, that state, as opposed to the state of the owner's residence, had a predominant right to tax;
- With respect to wealth derived from *business property* having a *fixed location*, and from *personal property* having a *close relation to land*, the considerations were similar to those involved in the case of land; therefore, the analysis favored the right of the source state to tax;
- With respect to wealth derived from *tangible personal property* not closely tied to land, source or situs often played little part in the value of the property and was, in fact, often determined arbitrarily; the state of the owner's residence, the state where the property presumably was enjoyed and which was usually also the state where rights in the property were enforced, enjoyed a predominant claim to "economic allegiance";
- With respect to wealth derived from a category of property identified as *corporeal moveables not ordinarily capable of a fixed location* (principally ships) the dominant claim to tax was ascribed to the state of registry, on the ground that that was the state which enforced property rights; the state of source often could not be identified;
- With respect to wealth derived from *intangible property*, considerations similar to those with respect to tangible personal property prevailed; these supported the primacy of the residence state, except in the case of real property mortgages, which were deemed akin to land;
- With respect to *earnings and salaries*, the residence state had virtually sole claim to "economic allegiance."

The report discussed four methods of avoiding double taxation. The first would unilaterally concede the primary right to tax to the source state. The second would concede exclusive taxing authority to the residence state, through exemption in the state of source. The third was a "proportionate division" method—dividing taxes between two states according to some predetermined formula. The fourth method was "classification and assignment"—classifying income according to type, and assigning primary rights to tax certain types of income to one state and other types to the other.

In formulating recommendations, the economists ruled out methods which accorded primary or exclusive taxing rights to the source state, largely on the ground that this would be contrary to modern progressive taxation based upon an "ability to pay" principle. Approaches based on proportionate division and classification and assignment were also rejected, because the economists judged the theoretical problems involved in these approaches to be too great. Their preference was for the second method—exemption by the source state of the income of nonresidents—both because it avoided theoretical complexities and because it accorded with what they viewed as economic reality: The source state should cede the right to tax when it sought investment from abroad. To the objection that this method would create an unbalanced treatment of "creditor" and "debtor" countries—the method would involve a substantial revenue sacrifice by the latter—the economists responded with a proposal to divide revenues based upon the relative magnitude of different types of income deemed to have originated in each state. The taxpayer would not be affected.

In 1925, a Committee of Technical Experts organized by the League issued a further report on problems of double taxation. The report distinguished between "impersonal" taxes—schedular taxes or taxes imposed on different types of income—and "personal" taxes, i.e., global taxes imposed on total income. With respect to personal taxes, the Experts recommended that the state of residence be accorded a right to impose a tax on all income. They further suggested, however, that the state of source also be assigned a right to tax income from real property, and income from agricultural, commercial, and industrial undertakings. When such dual taxation occurred, "relief" would be given in the form of a reduction of tax, calculated according to prescribed formulae, in the state of residence.

The report of the Technical Experts also addressed, for the first time, the problem of international tax evasion. On the basis of the few existing arrangements between

countries, the Committee concluded that "exchange of information in taxation matters" represented the best approach to combating such evasion.

In 1927 the Technical Experts issued the first international draft model treaties: A model income tax treaty, a model covering succession duties, and a model governing administrative assistance in the collection of taxes. These were followed in 1928 by five models issued by a General Meeting of Government Experts convened by the League to discuss the 1927 models. Three of these 1928 models were separate income tax models—one for use between states which employed both "personal" and "impersonal" income tax systems; a second for use between states wishing to cover only "personal" tax systems; and a third covering exclusively "impersonal" tax systems.

The 1928 models provided the framework for the negotiation of a wide network of tax treaties, particularly among European nations. The models also served as a framework for the earliest U.S. tax treaties.

From the foregoing review it is clear that what I have referred to as the fundamental policy questions in the tax treaty area were addressed at an early date. The first question—what tax treaties are intended to achieve—was considered in the first report of the economists: double taxation represents an unfair burden on existing investment, and an arbitrary barrier, destructive of international economic welfare, to the free flow of international capital, goods, and persons. Nations should seek to eliminate—or at least alleviate—it.

The second question concerned the choice of bilateral approaches to eliminating double taxation. The early work of the League—particularly its sensitivity to the imbalance between "creditor" and "debtor" nations and its consideration of differences between "personal" and "impersonal" tax systems—revealed the justification for bilateral approaches. Multilateral agreement is difficult when countries are in different economic or legal circumstances. Unilateral measures, on the other hand, are almost inevitably ineffectual. After the first international models were issued, the Hoover administration proposed modifications of the U.S. revenue laws under which the United States would have exempted income of any foreign person except realty and business income, if the foreign country of that person's residence granted reciprocal treatment. The idea was to avoid double taxation without separate international agreements. The measure was never enacted, but it is doubtful that it would have worked. Foreign investment by U.S. persons at the time was some four times greater than investment by foreign persons in the United States. Most countries would probably not have absorbed the revenue sacrifice involved in granting the "reciprocal exemption" envisioned by the bill.

Perhaps the most significant aspect of the League's work was its ultimate choice of "classification and assignment" as the basic structure for a model bilateral agreement. This structure is today universally used in virtually all tax treaties. While the League chose "classification and assignment" because of the differences between "debtor" and "creditor" countries, the approach has been used even between countries which believe that debts and credits between them are more or less in balance. The principal impact of this method is the need it imposes to classify and assign taxation rights, in negotiations, on an item-by-item basis.

In addition, the "economic allegiance" principle articulated in the League's work is the basis for most of the substantive rules—the actual classifications and assignments—in modern tax treaties. Real property income and income connected with a fixed business location are still the kinds for which a right to tax is most readily accorded to the source state. Passive investment income remains the kind which under international practice is most commonly reserved to the owner's state of residence.

## **B. The work of international organizations since 1928**

At the conclusion of its work, the General Meeting of Government Experts recommended that the League appoint a permanent Fiscal Committee to monitor the development of an international network of tax treaties. The most significant product of this Committee's early work was a model treaty approved in 1934, governing the attribution of profits among different components of an integrated enterprise operating in different states. This model set forth for the first time as an international standard

the so-called "arm's length" principle—that profits should be attributed to different components as if the components were separate enterprises dealing with each other at arm's length.

In 1943, the Fiscal Committee sponsored meetings in Mexico City which drafted new international models governing income taxes, estate taxes, and administrative assistance in collection. These "Mexico models" were substantially more detailed and precise than the 1928 models.

In 1946, the Fiscal Committee held another series of meetings in London; a model income tax treaty similar in structure and substance to the 1943 Mexico model, but more refined still, was drafted. Rules governing the double taxation of capital were introduced.

In 1956, acting at the urging of the international business community, the Organization for European Economic Co-operation (OEEC)—an entity devoted to the study and resolution of interstate economic problems facing European nations—formed a Fiscal Committee and charged it with the task of exploring the possibility of achieving a uniform multilateral treaty for the avoidance of double taxation. In its first report, in July 1958, the Fiscal Committee recognized that the task of preparing a multilateral treaty was "necessarily a long-term work"; it proposed first to issue a series of articles aiming at a "Model Bilateral Convention acceptable to all Member countries."

The Fiscal Committee proceeded to issue 30 articles in 5 installments, which were then collected as a model treaty in 1963. Meanwhile, in 1961, the OEEC was reconstituted as the Organization for Economic Cooperation and Development (OECD), with the addition of the United States and Canada. Other developed non-European countries, including Japan, Australia, and New Zealand, have since joined the organization.

The 1963 OECD model income tax treaty was accompanied by lengthy and elaborate commentaries which explained particular provisions. The commentaries also indicated matters not addressed in the model which might be covered in particular negotiations; the relationship of the model to the London and Mexico models, as well as the early work of the League; and the relationship of the model to prevailing practices of member states.

The OECD followed this work with the publication in 1966 of a comparable model estate tax treaty. In August 1977, the OECD issued a revised model income tax treaty, with revised commentaries, both updated in light of the experience of member and nonmember states in working with the provisions of the 1963 model. Currently, the OECD is endeavoring to revise the 1966 estate tax model, to incorporate in that model provisions with respect to gift taxes, and to produce a new model governing reciprocal administrative assistance in tax matters.

The OECD efforts were principally directed to tax treaty negotiations between developed countries. Shortly after completion of the first OECD model, the United Nations Economic and Social Council instituted efforts to develop principles for negotiations between developed and developing countries. In 1967, the Council adopted a resolution expressing the view that tax treaties between developed and developing countries could serve to promote the flow of productive investment to the latter, and noting that, despite the widespread proliferation of treaties between developed countries, there were still very few treaties between developed and developing countries. The Council, therefore, requested the Secretary General to establish an ad hoc group of experts to study the problem of tax treaties between developed and developing countries, and to recommend guidelines for the negotiation of such treaties.

The experts came from both developed and developing countries. They are recommended by their governments, but serve in their private capacities, rather than as representatives of their governments. Since 1968, the group has met on a regular basis, and has issued eight reports on its work to the Secretary General; the reports provide a comprehensive discussion of the kinds of problems raised by developed-developing country treaties. In 1974, the group issued preliminary guidelines for negotiations, which were superseded in 1979 by the issuance of a manual containing a new set of guidelines. The group intends in the near future to issue a model developed



country/developing country treaty, representing a refinement of the guidelines set forth in the 1979 manual.

### C. The 1977 OECD model

The OECD model can best be described for present purposes by a brief summary of its principal categories of rules.

*Taxes covered.*—All income taxes of the contracting states are covered, including taxes imposed by local authorities and political subdivisions. Capital taxes are also covered, and a separate article is devoted to such taxes.

*Personal scope.*—Coverage extends to residents of one or both of the contracting states. It does not generally extend to cases where both states claim a right to tax on a source basis, or to cases where one state taxes on the basis of citizenship.

*Source basis taxation of income from real property and permanent establishments.*—The OECD model retains the League principle that the source state should have the right to tax real property income. However, the model assimilates mortgage income to interest, not real property income. The model also allows a source state to tax business income fully if such income is attributable to a permanent establishment in the source state. This rule also descends from the early League work, but is now subject to exceptions which have evolved over time; moreover, there are special provisions for cases where business is conducted through an agent, providing for insulation from source basis taxation where the agent is independent and for such taxation when the agent is dependent but conducts significant business on behalf of the enterprise. The allocation rules used in these provisions explicitly rely upon the “arm’s length” principle. A special exception for international transportation income grants exclusive taxation rights to the state where the “center of effective management” of the enterprise is located.

*Passive investment income.*—With respect to dividends and interest, the OECD model adopts the device of a limited or partial right to tax at source. Dividends may generally be taxed by the source state at a rate no higher than 15 percent; if, however, the payee is a corporation controlling more than 25 percent of the capital of the payor, the dividends are taxable at a maximum 5-percent rate. This special reduction is designed to harmonize with features of the laws of many states giving relief from double corporate level taxation for intercorporate distributions. The interest article reserves to the source state a right to tax at a rate no higher than 10 percent of the interest payment. The royalty article provides for reciprocal exemption of royalties at source.

With respect to capital gains, the model generally reserves the right to tax to the state of residence, with the exception of property closely associated with the source state, land and permanent establishment business property. Taxation of gains from the disposition of ships and aircraft used in international operations is reserved to the state in which the centre of effective management of the enterprise is located.

*Personal service income.*—The general rule in the OECD model is that personal service income is taxable in the state where the services are performed; but there are also a variety of special rules. With respect to “dependent” services, the state of residence has exclusive taxing rights as long as the taxpayer was present in the other state for less than half of the taxable year, and was not working under conditions such that the other state would likely be obliged to allow a deduction for his salary. “Independent” services, on the other hand, are taxable only to the extent they are connected with a “fixed base” in the source state, a concept which parallels the permanent establishment criterion used for determining when business profits may be taxed at source. Directors’ fees are taxable in the source state; i.e., the state of the paying corporation’s residence. Artists’ and athletes’ income is invariably subject to taxation in the state where the personal services are rendered; and if the income from such services is deflected to another person, that person may be taxed in the source state without regard to whether it has a permanent establishment or fixed base there. Pensions are taxable only in the state of residence; income from government service generally in the state paying the income; and a special provision exempts payments to students for their maintenance, education, or training.

*Nonclassified income.*—The OECD model ultimately recognizes the primacy of the residence state in two ways. First, unclassified income, not specifically covered in the model, is taxable exclusively by that state. Second, a residual right to tax is generally accorded to the state of residence, even when the primary right to tax is granted to the source state. The residence state is required to bear the burden of eliminating double taxation for any income assigned to the source state; but it may tax the income in full if the source state does not tax it, or does not tax it at a level equal to that of the residence state.

*Methods of avoiding double taxation.*—The OECD model provides for alternative methods of avoiding double taxation. The first, the “ordinary credit” method, is patterned on the U.S. foreign tax credit provisions. The residence state allows a reduction of its tax for the tax paid the other state, but is not required to allow a greater reduction than an amount bearing the same proportion to its total tax as the amount of income which the source state is allowed to tax bears to the taxpayer’s total income. The second method, “exemption with progression,” requires the residence state to exempt the income which the source state may tax, but permits the residence state to determine its tax on remaining income by a progressive schedule which takes account of the income taxable by the source state.

*Nondiscrimination.*—This provision forbids states from discriminating against nationals of the other state in tax matters—it guarantees the principle of “national treatment.” Nondiscrimination provisions were common in tax treaties from an early period, but the 1963 OECD model introduced two novel forms of such provisions. The first forbids discrimination against a “permanent establishment” of a national of the other state. The second forbids discrimination against an enterprise based on the fact that its capital is owned in substantial part by nationals of the other state.

*Exchange of information.*—The OECD model contains relatively liberal exchange of information provisions, which, however, include limitations deriving from the early work of the League: the restriction to information in the requested state’s possession, or available under its laws; and a guarantee that a requested state need not take steps contrary to its security, sovereignty, or public policy.

*Mutual agreement procedure.*—The model provides a mechanism for the resolution of disputes; each state designates in the treaty a “competent authority” who serves as its representative for interpreting and implementing the treaty. The model provides for consultation among competent authorities, but does not require that they come to an agreement, nor does it provide any mechanism for binding them to a decision. The procedure is supplementary to procedures, including recourse to courts, which are available to a taxpayer under domestic law.

## II. U.S. Treaty Policy

### A. Existing U.S. treaties

The United States presently has 30 independently negotiated income tax treaties in force. Several of these have been extended to territories of the treaty partner, and in some instances these territories have since become independent and assumed their obligations under the treaty. While a comprehensive review of U.S. treaties is not possible here, a general survey may be useful.

In part because U.S. treaties have been heavily influenced by the international models outstanding at the time of their negotiation, and in part because they have been influenced by developments in domestic law, the treaties tend to follow patterns corresponding to the periods when they were negotiated. Roughly speaking, there are four principal “periods.”

The first general U.S. tax treaty—after certain limited purpose treaties, chiefly governing the taxation of shipping profits—was with France, signed in 1932. The principal purpose of this treaty was to mitigate the broad territorial reach of French taxation of U.S. business enterprises operating in Paris. The treaty did not deal generally with many of the subjects covered by the 1927–28 League models. It contained rules governing only income from government service; war pensions; private pensions and annuities; royalties; and business profits. The treaty contained no provisions concerning administrative cooperation or exchange of information; and none governing nondiscrimination.



Much broader was a treaty signed by the United States with Sweden in 1939, and a new treaty signed in the same year with France. The Swedish treaty was ratified in 1940, but the French treaty, which replaced the 1932 treaty entirely, was not ratified until the end of the Second World War. In these two treaties, the United States established some important principles which have remained cornerstones of U.S. tax treaty policy. The first was that tax treaties should not generally affect the taxation by the United States of its citizens and residents. The second was the emphasis given to administrative cooperation, particularly exchange of information. The U.S. system of collecting income taxes depends heavily upon an ability to collect information at source on payments of income, and sometimes to collect taxes at source; and our ability to obtain information concerning a person's financial activities from third parties. In the Swedish and French treaties, the United States recognized the special importance to us of obtaining access to information at source when the source was in another country.

In 1942, the United States signed a general treaty governing double taxation and administrative cooperation with Canada. This treaty differed from the 1939 treaties with France and Sweden in that it covered generally items of investment income; the French and Swedish treaties did not apply, in particular, to interest income.

These treaties—with France, Sweden, and Canada—represent our “early period” conventions. The 1939 treaty with France was superseded by a new treaty signed in 1967, which itself was subject to substantial revision by 1970 and 1978 protocols. The 1939 Swedish treaty was substantially revised by a 1960 protocol, but the treaty signed in 1939 is still in effect, and is our oldest. The 1942 Canadian treaty was substantially revised in 1950; but it, too, is still in effect.

The “second period” of U.S. income tax treaties was inaugurated with the 1945 treaty with the United Kingdom. This treaty generally covered items of passive investment income—interest, royalties, dividends, capital gains—but distinguished among particular categories of such income. Notably, it provided for exemption of interest from tax at source. The treaty was regarded as a major advance for the United States because of the United Kingdom's acceptance of broad exchange of information and administrative cooperation provisions. This treaty was substantially revised by a protocol negotiated in 1966, and ultimately was replaced by a new treaty signed in 1975, which, with one exchange of notes and three protocols, entered into force just 4 days ago. The original treaty remains in force, however, with approximately 15 jurisdictions with respect to which it was extended, with modifications, in 1958.

The first United Kingdom treaty established a model for U.S. treaties negotiated between the end of World War II and the commencement of double tax treaty work by the OEEC and, later, the OECD. During this period we negotiated treaties with most of the states of the developed world, including 12 treaties with European countries (the United Kingdom, the Netherlands, Denmark, Norway, Ireland, Greece, Switzerland, Italy, Germany, Austria, Finland, and Belgium); 4 with non-European developed countries (South Africa, Australia, Japan, and New Zealand); and 1 with a developing country (Pakistan). The treaties with Japan and Finland were superseded by new treaties in the early 1970's. The treaties with the United Kingdom and Belgium were also superseded insofar as the developed country treaty partner is concerned, but remain in force with respect to territories or former territories of those countries. And several other treaties of this period have been substantially revised by protocol.

The treaties negotiated in this general period cover the basic range of subjects in the present OECD model and the present U.S. model, although there are omissions in some of them. But the content of some of these treaties often differs from what we would seek today. Among these differences the most important concerns the typical “business profits” article. Before 1966, domestic law made the United States a “force of attraction” jurisdiction; i.e., if a foreign person was engaged in trade or business in the United States, *all* his U.S. source income was subject to tax, regardless of whether the income was attributable to the business; and we taxed *none* of that person's foreign source income even if, in an economic sense, such income was attributable to the U.S. business. In accordance with this statutory law, most of our treaties from this period provided that permanent establishments could be taxed in a source state on, and only on, income arising in the source state. When we changed our law in 1966, in addition to relieving non-“effectively connected” income from U.S. tax, we also subjected to



tax "effectively connected" income having a foreign source. The existing treaties undermine the current statutory pattern of taxation, because by statute we no longer tax the noneffectively connected U.S. source income—even though we have the right to do so by treaty—while the treaties preclude us from applying our domestic law to tax effectively connected income of foreign source.

Most of the treaties of this period allow a person earning real property income in the United States the right to elect annually to be taxed on a "net basis"; i.e., at progressive rates and with deductions, rather than at the gross (30%) rate applicable in the absence of an election. The Internal Revenue Code has permitted such an election since 1966, but that election is *irrevocable* unless consent to change is given by the Internal Revenue Service. Treaty provisions permitting the election to be made on an annual basis create certain tax avoidance opportunities for persons investing in U.S. real property.

Most of these treaties also concede the right of the United States to impose its "second dividend" and "second interest" taxes, the taxes we apply to dividends and interest paid by foreign corporations doing substantial business in the United States. Most contain personal service articles different in significant detail from those we would seek today; few contain the special provisions now included in U.S. treaties governing the earnings of artists and athletes. Most have exchange of information and mutual agreement provisions that are more restrictive than we like to negotiate now. Most have imprecisely drafted provisions governing the mechanism for crediting "source country" taxes. Most contain provisions conferring benefits upon teachers, which we no longer view as appropriate. Although many of these treaties have been modified by subsequent protocols or new treaties, many outdated provisions continue in force.

This "second period" of the U.S. tax treaty program also witnessed the entering of a tax treaty relationship with smaller countries. Under the Mexico and London models, a treaty could be extended to territories of one of the parties by notice given through diplomatic channels to the other party. Our 1945 treaty with the United Kingdom contained such a "territorial extension" provision, as did several other treaties signed shortly after the World War II. In the process of seeking ratification of those treaties, however, understandings were reached between the executive branch and the Senate Foreign Relations Committee that no such extension would be effected without separate ratification of each extension by the Senate. In 1955, pursuant to a request by the Kingdom of the Netherlands, the United States for the first time extended a tax treaty to an overseas territory of a treaty partner: the Netherlands Antilles. In 1957, the Belgian treaty was extended to three Belgian territories which are now Rwanda, Burundi, and Zaire. In 1958, the United Kingdom treaty was extended to 20 overseas territories of the United Kingdom.

At the same time, the United States, under the Eisenhower administration, inaugurated a program of negotiating tax treaties which included a "tax sparing" provision. Many developing countries have, in the past and at present, relied upon special tax incentive legislation to attract foreign investment. The idea of "tax sparing" developed in the 1950's: under this concept, a developed country would agree by treaty to give a credit not only for taxes imposed by a developing country, but for taxes which would have been imposed in the absence of tax holiday legislation. This idea won widespread support among business groups interested in the double taxation problem such as the National Foreign Trade Council and the International Chamber of Commerce.

When the first U.S. treaty with such a provision, the treaty with Pakistan, was submitted to the Senate for ratification, the "tax sparing" idea was greeted with hostility by the Foreign Relations Committee. The Senators emphasized the traditional view of U.S. tax treaties—that they did not reduce or affect the tax burdens of United States persons—and that tax sparing was obviously a departure from this principle. While the Pakistan treaty was under consideration, however, Pakistan repealed its tax incentive legislation, which mooted the treaty provision. Nevertheless, the Committee, in reporting the treaty favorably, entered a reservation to the tax sparing provision, and the treaty was approved by the Senate subject to the reservation. Three other treaties with tax sparing provisions—with India, the United Arab Republic, and Israel—were never reported out by the Committee.

The third group of U.S. treaties comprises those 12 treaties in force that were negotiated since 1960, but prior to publication of the U.S. model treaty in 1976. Of these, six (Luxembourg, France, the United Kingdom, Japan, Belgium, Iceland, and Finland) are with OECD countries; two (Korea, Trinidad & Tobago) are with Free World developing countries; and three (the U.S.S.R., Poland, and Romania) are with Communist countries. In addition, the United States during this period negotiated significant protocols to some of the earlier treaties notably those with Germany, Sweden, and the Netherlands.

Several features distinguish these treaties from those of the prior period. With the exception of the quite unusual treaty with the U.S.S.R., these treaties tend to follow closely the structural format of the international model; but they contain special provisions, found neither in the earlier treaties nor in the OECD model, reflecting a unique approach by the United States. The most important of these provisions are those dealing with "general rules of taxation" and source of income. The general rules of taxation provide, typically, that the treaty is not to restrict any allowances, credits, or deductions permitted under domestic law; and that a contracting state is permitted to tax the income of a resident of the other contracting state only to the extent that income is from sources within the first state. The source provision includes detailed rules governing when income is deemed to arise in the source state; these rules, which typically expand to some extent upon the "source" rules set forth in the Internal Revenue Code, are designed to guarantee that the classification and assignment of substantive taxing rights will avoid double taxation in practice.

This "third period" of U.S. tax treaties saw another significant development in regard to U.S. tax relations with developing countries. Under the Kennedy and Johnson administrations, the Treasury did not negotiate treaties with "tax sparing" provisions, because it viewed those provisions as creating an artificial bias in favor of foreign investment over domestic investment. In 1962, however, Congress adopted a statutory investment tax credit which, by its terms, was available only for investments in property placed in service in the United States. The Treasury, by treaty with developing countries, agreed to allow a similar credit for property placed in service in the developing country treaty partner, and treaties containing such provisions were signed with Thailand, Brazil, Israel, and the Philippines. This provision, too, was found unacceptable by the Foreign Relations Committee, which viewed the investment tax credit as designed to spur domestic investment and domestic employment, and which regarded it as inappropriate to extend the measure by treaty to stimulate foreign investment. Of the treaties which contained an investment tax credit feature, the Committee reported only the one with Brazil, subject to a reservation on this point; the Senate approved the treaty subject to the reservation, but the treaty never entered into force.

The fourth group of U.S. treaties are those based more firmly on the 1976 U.S. model and the revised version of that model published in 1977. Only one treaty currently in force, with Hungary, falls in this group. But there are numerous treaties currently in the process of negotiation, translation, signature, or ratification that would fall in this group as well.

## B. The U.S. model

The point of reference for all U.S. income tax treaty negotiations undertaken today is the U.S. model income tax treaty, which follows the OECD model in most important respects. Issued publicly for the first time in December 1976, the model was reissued, with relatively minor modifications, in May 1977. Although some U.S. negotiating positions have changed since 1977, a new version of the model has not yet been issued. We attempt to take developments into account in actual negotiations.

The most important differences between the U.S. model and that of the OECD are as follows:

*Citizenship basis taxation.*—The OECD model applies only to states which tax globally on the basis of domicile or residence. We, of course, tax on a citizenship basis in addition to a residence basis. We regard it as appropriate to attempt to relieve double taxation which occurs when a nonresident U.S. citizen is taxed on a source basis by a treaty partner. In addition, the U.S. model contains a "saving" clause

permitting taxation of U.S. citizens (including former citizens) as if no treaty were in effect. Since this rule is overbroad in certain respects, it is necessary to accompany the saving clause with specific exceptions.

*Coverage of state and local taxes.*—Under the U.S. model, state and local income taxes are not covered, except for the nondiscrimination article. The OECD model provides for general coverage of the taxes of a political subdivision or local authority.

*Corporate residence.*—The United States treats place of incorporation as the test of corporate residence, and the U.S. model reflects this statutory rule. Some other countries use a “managed and controlled” test. The OECD model provides that when a corporation is, under the domestic law of the contracting states, deemed a resident of each state, its residence is determined by the place where its “effective management” is situated. The U.S. model resolves such cases on the basis of place of incorporation.

*Interest exemption.*—The U.S. model contains a reciprocal exemption of interest at source. The OECD, in contrast, grants a right to the source state to tax at a rate not in excess of 10 percent.

*Investment or holding companies.*—The U.S. model contains a provision not found in the OECD model, denying reductions of source basis taxation when a corporation of the other state is largely owned by nonresidents of that state and benefits in that state from special tax measures. This provision, which places the United States at the forefront of the international effort to prevent treaty abuse, requires further thought and refinement.

*Elimination of double taxation.*—The U.S. model contains detailed provisions for relief from double taxation, and an explicit assurance of a foreign tax credit for taxes covered. Source rules are provided to permit the classification and assignment of substantive taxation rights to operate effectively. The model does not extend relief for the deemed paid credit below the first foreign subsidiary.

Beyond these fundamental differences between the models lie a wide range of other differences. Some are merely matters of style, although an effort has been made to minimize differences without substance, for the sake of facilitating negotiations. An additional list of significant points in the U.S. model would include at least the following:

*Penalty taxes.*—The model does not cover the accumulated earnings tax and the personal holding company tax. We wish to ensure that U.S. persons do not evade these penalty taxes through the formation of corporations in treaty countries.

*Excise taxes on insurance premiums and private foundations.*—The U.S. model covers these taxes, on the theory that they are, in effect, imposed in lieu of income taxes. In cases where the other country has similar taxes, we would insist upon reciprocity.

*Coverage of taxes for nondiscrimination and exchange of information provisions.*—The U.S. model covers all taxes, including state and local taxes, for purposes of the nondiscrimination article. It covers all national level taxes for purposes of the exchange of information article. The first of these provisions represents a strong U.S. position against discriminatory tax measures. Since there is a long tradition in the United States of state adherence to standards of nondiscrimination, we attempt to secure comparable coverage by the treaty partner. With respect to exchange of information, we believe that since a treaty relationship is to be established, the broadest possible provisions for information exchange are desirable; but even if this notion is unacceptable to the treaty partner, at a minimum we wish to obtain sufficient information to permit the treaty to operate, even if the information was obtained by the treaty partner under a national level tax not generally covered by the treaty.

*Trusts and partnerships.*—Unlike the OECD model, the U.S. model contains rules ascribing a state of residence to trusts and partnerships. These rules are intended to permit the treaty to operate in circumstances that are relatively common in U.S. practice.

*Remittance basis.*—Reductions in source basis taxation are generally not justified in the face of rules in the residence state preventing taxation of the benefited income. Many countries—particularly countries previously forming part of the Commonwealth of the United Kingdom—provide by law that residents will not be taxed on income which is not remitted to the country. The U.S. model denies reductions in source basis taxation in such circumstances.



*Construction projects.*—The model provides that a construction project will not be considered a permanent establishment, and thus subject to taxation at source, until it lasts for more than 24 months in the source state. This provision reflects the U.S. position as a net exporter of construction services. The comparable OECD provision is 12 months; the U.N. model prescribes a period of 6 months.

*Net basis election for real property.*—The U.S. model, reflecting statutory law, permits a taxpayer to elect to be taxed on real property income on a net basis. This rule is included in the model to ensure that the other state will allow similar net basis taxation. We are prepared to delete this rule when we are satisfied, through negotiations, that the statutory law of the other state permits such taxation.

*Allocation of expenses to permanent establishment.*—The U.S. model contains more detailed rules than the OECD model governing the allowance of deductions in the source state for expenses borne by a home office on behalf of the entire enterprise. This provision is designed to reflect U.S. rules governing allocations of expenses to foreign source, as opposed to domestic source, income.

*Definition of business profits.*—The U.S. model contains a rule defining business profits, and making clear that rentals of tangible personal property and income from the licensing of films and broadcasting rights come within the definition. We seek a definition of business profits because the OECD model is ambiguous in regard to certain kinds of income. We prefer to classify film and broadcast income, and income from the leasing of tangible property, as business income, because this classification ensures taxation at source, if there is to be such taxation, on a net basis. The expenses associated with these kinds of income can be high. In contrast, the OECD model classifies these types of income as royalties, but provides for exemption at source.

*Expanded definition of shipping and air transport income.*—The U.S. model expands the concept of income from international shipping and air transport to cover the rental of ships, aircraft, and containers used in international transport. We believe that the income from such activities is essentially similar to income from international shipping and air transport, and that the policies dictating a separate provision for the latter types of income apply equally to the former.

*Direct investment dividends.*—The U.S. model provides for a maximum rate of 5 percent for source basis taxation of dividend income derived by a corporation owning 10 percent or more of the voting stock of the company paying the dividends. The comparable rule in the OECD model provides for a maximum 5-percent rate when the payee corporation owns 25 percent or more of the capital of the company making such payments. The U.S. preference for a 10-percent-ownership test is designed to mesh with U.S. statutory law governing the deemed paid foreign tax credit.

*Second withholding taxes.*—The U.S. model permits the United States to impose its “second withholding taxes” on dividends and interest paid by a foreign corporation deriving income from the United States. These rules are particularly important in negotiations with a country having a “branch profits” tax.

*Royalties.*—The U.S. model provides that royalties include gains contingent on the productivity, use, or disposition of rights or property. This rule corresponds roughly with U.S. statutory law.

*Capital gains on the disposition of shares in a real property holding organization.*—This is one respect in which our current negotiating practice deviates from the model. Under both our model and the OECD model, a source country may tax capital gains on real property. But an investor may avoid source state taxation by incorporating a holding company to own the property. This device will not insulate operating income from current taxation, but it may be effective for avoiding source taxation of capital gain on sale of the shares, which may well reflect appreciation in the value of the underlying property.

U.S. statutory law does not generally tax foreign investors on gains from the disposition of shares in corporations formed to hold real property. In connection with the Revenue Act of 1978, however, legislation was proposed which would have taxed gains from the disposition of shares in a company formed to hold U.S. farmland. In the 96th Congress, more far-reaching legislation has been introduced which would tax foreign investors on their gains from the disposition of shares in real property holding organizations—entities formed to hold any U.S. real property. The legislation has had

broad congressional support; and the Treasury has supported the general idea behind it.

In the face of these developments, we have modified our treaty policy and now seek a provision granting reciprocal rights to source state taxation of capital gains on the sale of shares in corporations formed for the sake of holding real property situated in that state.

*Independent personal services.*—The U.S. model allows source basis taxation when a person is present in the source state for more than half of a taxable year. This provision, which derives from U.S. statutory concepts, is similar to the dependent personal services provisions in both the OECD and the U.S. models. It is intended to supplement the “fixed base” rule which the OECD model uses exclusively for independent services and which is sometimes difficult to administer.

*Directors’ fees.*—The U.S. model contains no separate article on this subject, reflecting the view that directors’ fees should be taxed as independent personal services or dependent personal services, as the case may be. Many other countries have special statutory rules for directors’ fees, because such fees are not deductible by the paying corporation. They are, in effect, considered a distribution of corporate profits.

*Artists and athletes.*—The OECD model provides that the state where services of an artist or athlete are rendered may tax the income from such services without limit. It also provides that where income from such services is diverted to another person, the source state may tax without regard to the existence of a permanent establishment or fixed base. The U.S. model, in contrast, contains a “threshold” limiting source state taxation when an artist or athlete has not received remuneration in excess of \$15,000 in the taxable year. It also limits the special rule on source state taxation of diverted income to cases where the performer has an interest in the recipient entity.

*Social security payments.*—The OECD model reserves to the residence state the right to tax pensions, including benefits paid from a public social security fund. The U.S. model provides for exclusive taxation of social security and other public pensions at source. Since the United States does not tax social security benefits, and has geared benefit levels accordingly, we seek to ensure that our benefit structure will not be impaired by taxes imposed by the other state.

*Annuities, alimony, and child support.*—The U.S. model contains specific provisions, missing from the OECD model, to deal with these items of income. With respect to annuities and alimony, the U.S. model provides for exemption in the source state. With respect to child support, the model—reflecting U.S. statutory law, which does not provide for taxation of such payments—provides for exemption in both states.

*Government service.*—The U.S. model follows the OECD model in this article, except that it contains a rule treating the spouse or dependent child who begins to render government service after moving abroad like the spouse who moved abroad for the purpose of rendering such service. In addition, the U.S. model provides that a citizen rendering government service will generally be treated as a resident of the sending state for all purposes under the treaty.

*Students.*—The U.S. model provides an election for a student to be treated for tax purposes as a resident of the state in which he is studying. This provision is intended to permit the student to take advantage of statutory allowances and exemptions available only to residents. A person who makes such an election is required to pay tax on his worldwide income to the United States.

*Nondiscrimination.*—The U.S. model covers discrimination against nonresidents but provides that, in effect, nonresident aliens will not be entitled to net basis taxation in the United States. In addition, the model provides a relatively detailed rule governing the allowance of indirect expenses as deductions in the source state. In these respects the U.S. model extends principles found in the OECD model. On the other hand, the U.S. model—unlike the OECD model—provides no protection against discrimination by the source state for corporations not having a permanent establishment in that state.

*Mutual agreement.*—The U.S. model provides for no time limit on the period in which a case can be presented to the competent authority, and spells out in detail some of the actions which are permissible for the competent authority to take. We think it helpful to provide as much guidance to the competent authority as possible. Many countries, which have more flexible competent authority mechanisms than the United



States, do not perceive the need for such rules, which are not found in the OECD model.

*Exchange of information and administrative assistance.*—The U.S. model provision on exchange of information is broader than that of the OECD. It expressly requires a state of which information is requested to take depositions, and engage in other specified information-gathering activities, on behalf of the requesting state. The U.S. model is intended to produce information in a form that will be useable in U.S. courts. It also contains a provision requiring the residence state to collect taxes on behalf of the source state for the purpose of ensuring that relief granted by the source state does not inure to the benefit of persons not entitled to such relief. This feature is aimed at combating the use of nominees to secure unintended advantages under a treaty.

*Territorial extension.*—The U.S. model contains no provision like that of the OECD model governing territorial extensions. Since territorial extensions must be independently ratified in the United States, a territorial extension provision is of no effect and, indeed, can be misleading.

The U.S. and OECD models are, of course, blueprints for only the issues commonly faced in treaty negotiations. There are many treaty issues which do not fit within the confines of the models. These issues arise either from special features in the other country's law or in our own, or from the status of the treaty partner—as a developing country, for example. As might be expected, these are some of the most serious and controversial issues we confront.

*Imputation systems.*—In recent years a number of developed countries have modified their pattern of taxing corporate earnings in order to mitigate "double taxation" at the corporate and shareholder levels. This "integration" of corporate and shareholder taxation has taken a variety of forms. In some countries, distributed profits are taxed at a lower rate than undistributed profits. In others an "imputation" system is used. Imputation means that part or all of the tax charged to the corporation is allowed as a credit to the shareholder when profits are distributed as a dividend; the shareholder includes in income both the dividend and the amount of creditable tax, and claims a credit against his individual liability for the tax paid by the corporation.

Imputation itself has various manifestations. Some countries have adopted "compensating" taxes at the time of a distribution, or at the time of a distribution of previously untaxed profits, to ensure that the shareholder credit is funded by taxes paid by the corporation. Some countries allow shareholder refunds when the credit at the individual level exceeds the shareholder's tax liability. Some countries have combined split rate systems with an imputation feature. Some countries impute only a relatively small portion of corporate level taxes to the shareholder. Some countries maintain substantial residual taxes at the shareholder level. The variations on this theme are many and complex.

In most cases, however, imputation countries, by their domestic law, do not accord the shareholder tax credit to nonresidents. Nonresident shareholders are ordinarily taxed at a flat percentage of the dividend. Imputation systems thus place our investors at a disadvantage, in terms of access to capital, by comparison with investors who are residents of the imputation country. We have sought in treaty negotiations to secure benefits for U.S. investors commensurate with the imputation benefits granted to source state investors. This may involve "imputation credits," or some substitute for them, for our residents who make equity investments in such countries. The issue gives rise to controversy and complexity in current negotiations.

*Tax sparing.*—A major issue, in negotiating with developing countries, concerns "tax sparing," the grant by the state of residence of a tax credit for taxes that would have been charged in the source state but are not because of special tax relief or "tax holiday" provisions. The position of developing countries is now as it was two decades ago—that tax holidays are in their national interest and that without tax sparing a credit country such as the United States—which allows the credit only for foreign taxes actually paid—counteracts the tax holiday legislation and itself collects the tax "spared."

We think it inappropriate to use tax treaties to favor foreign investment over domestic investment. Moreover, given the history of this issue, we believe that a treaty reflecting a different view would be unlikely to achieve ratification.



*Source basis taxation in developing countries.*—The OECD and U.S. models are, as indicated, designed primarily for treaties between countries where the flows of income and capital are roughly reciprocal. The limitations of source state taxation in those models produces a revenue cost for that state. However, when investment flows are more or less reciprocal, the revenue sacrifices more or less offset each other. In a treaty between a developed and a developing country the flows are largely in one direction: income flows from the developing country to the developed country. Thus, a model which is in form reciprocal in fact can impose a substantial revenue burden on a developing country. The U.N. guidelines, which contain a more expanded source basis of taxation, recognize the need of developing countries to conserve revenues. The shift is, however, tempered by the often conflicting need of developing countries to attract capital, an objective which is best served by limited source basis taxation.

*Permanent establishment definition and business profits.* The U.N. guidelines include an expanded definition of the permanent establishment concept. It permits taxation by the source state if an enterprise maintains a stock of goods for delivery in that state; or if it has an agent there who regularly makes deliveries on behalf of the enterprise. It permits a limited "force of attraction" of nonattributable income at source. And it contemplates source taxation of a foreign enterprise engaged only in purchasing in the source state.

*Shipping.* The U.N. guidelines contain an optional provision allowing source state taxation of shipping activity which is more than casual, even if that activity is conducted by an enterprise managed outside that state's borders.

*Investment income.* With respect to dividends, interest, and royalties the U.N. guidelines provide for a positive rate of taxation at source, but do not fix the maximum rate; the participating developing countries believed the OECD rates—5 percent on direct investment dividends, 15 percent on portfolio dividends, 10 percent on interest, and zero on royalties—were too low. With respect to capital gains, the U.N. guidelines reserve the right of the source state to tax shares representing a substantial participation in a company engaged in business within that state.

*Personal service income.* The U.N. guidelines treat managerial salaries as taxable in the state of a company's residence, regardless of where the managerial services are performed. They contain an option to allow source state taxation of pensions.

*Other income.* The U.N. guidelines limit residual residence state taxation to income from sources in the state of residence or from third countries; the source state is permitted to tax residual income arising, under its own laws, in that state.

The United States has long recognized that items that would likely be exempt at source in a developed country treaty may be taxable at source in a treaty with a developing country. In negotiating with developing countries we have sought primarily to shift items that such countries might prefer to tax on a gross basis into net basis taxation, since we believe net basis taxation to be both fairer and more reasonable than gross basis taxation. These points, of course, imply a broadened definition of "permanent establishment" in treaties with developing countries, and this coincides with a basic thrust of the U.N. guidelines.

The United States has also been prepared to accept relatively low thresholds for taxation of services income at source. And we have accepted relatively high source taxation of passive income in developing country treaties, focusing more on the practical need to avoid excess foreign tax credits than on the theoretical preference for residence basis taxation of such income.

As a very general matter, therefore, many of the U.N. guidelines appear acceptable as they stand, or with relatively minor revisions. We intend to draw heavily upon them in producing internal guidelines for use in negotiations with developing countries.

*Foreign tax credit.*—In June 1979 the Internal Revenue Service issued proposed regulations setting forth standards for determining when a payment to a foreign government constitutes an "income tax," or a tax in lieu of an income tax, creditable against U.S. tax liability under the Internal Revenue Code. These standards would preclude credits in the case of certain taxes which are viewed, or at least labeled, as "income taxes" by the governments imposing them. The regulations have doubtless highlighted questions regarding the extent to which tax treaties should, and do, guarantee foreign tax credits for the taxes they cover. These questions are especially

acute with respect to payments to foreign governments in connection with the exploitation of natural resources. It is our present policy to accord a treaty credit for covered taxes, and in some cases this implies a credit in cases where there may be doubt regarding the application of the statute. In such cases of doubt we believe the treaty credit should be limited so that it will have no effect for source state credits exceeding the tentative U.S. liability with respect to income arising in that state.

*State taxation using the unitary apportionment method.*—The “arm’s length” method of apportioning profits among components of an integrated international enterprise has been the international standard since the 1930’s. Within the United States, among states, a “unitary apportionment” method is still widely used. Many foreign countries have strongly objected to this method of state taxation when it is applied to foreign controlled corporate groups. They have argued that the method results in taxing more profits than are attributable to activities conducted within a state, and that it requires a burdensome amount of information about an enterprise’s worldwide operations.

*Third country use.*—Most U.S. treaties allow benefits in the nature of reductions in source basis taxation to corporations organized in the treaty partner, regardless of whether the owners of the corporation are residents of, or are in any other way connected with, that country. Any treaty conceivably can, therefore, be used to effect an overall change in the incidence of U.S. taxation of U.S. source income, by the simple formation of a “holding company” qualifying for treaty benefits. If a person, for instance, holds equity securities subject to our 30 percent withholding tax on dividends, he can normally reduce that tax by organizing a corporation in a country with which we have a treaty reducing the rate to 15 percent.

In practice, however, this kind of “third country use” of tax treaties does not routinely arise, because it is ordinarily not cost free to make investments through a holding company specially organized in a treaty partner. Most treaty partners of the United States will tax income received by the corporation, which ordinarily will eliminate any advantage from the reduction of the U.S. rate at source. To the extent the investor will be subject to withholding tax on payments from the corporation, or to the extent he is not able to claim complete relief in his home country for a dividend from a foreign corporation, the additional tax burden will often exceed the benefits achieved under the treaty with the United States.

This protection of the treaty process depends, however, on the existence of normal taxing provisions in the law of the treaty partner. Some of our treaty partners have special provisions granting privileges to holding companies, which result in reduced taxation of the holding company or reduced taxation on the payment of income from the treaty country to a third country. Sometimes this occurs for reasons of domestic policy, but sometimes the treaty partner has deliberately enacted provisions with the aim of attracting “offshore” business, with an eye to the revenues that can be collected from licensing fees or those taxes which are imposed; and to the service industry that can be built up around an “offshore” financing business.

In addition, treaties can be used to channel benefits to “third country” beneficiaries through the use of “conduit” companies. This practice depends upon an exemption from source basis taxation of payments from that country, and an hospitable attitude toward “offshore” business. The conduit company earns income in the United States which is subject, under the treaty, to reduced U.S. tax; the income is then siphoned off as payments deductible from the base subject to tax in the treaty partner, to the person who is the real investor.

These “treaty shopping” practices are objectionable for a number of reasons which I have previously described to this Subcommittee. The practices cause unintended revenue loss, not contemplated by the treaty “bargain.” They may undermine the willingness of third countries to enter into treaty negotiations with us. And, perhaps most seriously, such practices are contrary to the spirit of international double tax treaties, and enhance opportunities for international tax evasion. Double tax treaties are, as I have mentioned, founded on the principle of allocating taxing rights based on “economic allegiance”; treaty shopping accords a revenue power to a third country, the “base country,” which has little or no claim to such allegiance. In addition, since most “base countries” have local law provisions which ensure confidentiality of the identity of the ultimate investor, the conclusion is inescapable that the practices are employed to a large extent by persons evading taxes in their home country.



Within the last year we have initiated negotiations aimed at modifying three treaties which we believe present treaty shopping problems—with Switzerland, the Netherlands Antilles, and the British Virgin Islands. Our objective in these negotiations, generally, is to secure new provisions that will eliminate or materially reduce the potential for abuse.

There are potential statutory solutions to the “treaty shopping” problem. Congress could enact a law denying benefits under income tax treaties to corporations disproportionately owned by third-country interests, or to income used to a disproportionate extent to satisfy third-country claims. Switzerland has a law like that, but it is aimed at persons using Switzerland as a base country to derive income from countries with which Switzerland has tax treaties, not at persons earning income in Switzerland. Such legislation by the United States would require careful assessment. Statutory override of treaty bargains has a disruptive effect on our entire treaty program, if not on our foreign relations generally. Moreover, a blanket denial of benefits to corporations controlled by third country residents would undoubtedly cut too broadly since our principal difficulties stem only from a few treaties with countries which have chosen to foster an “offshore” business as a deliberate policy. Such legislation might deny benefits to arrangements having legitimate business purposes.

*Coverage of possessions.*—A number of our negotiations have raised the question of treaty coverage of U.S. possessions. At present, none of our treaties in force applies to any of the possessions. The possessions have income tax systems which are separate from the U.S. system, although the law in force in many of them is the Internal Revenue Code as “mirrored”; and in others, the law is closely patterned on our internal tax law. We generally believe that covering the possessions is a salutary idea, because it secures the protections of a treaty for possessions residents who wish to invest or otherwise earn income abroad, and it may contribute to increased investment in the possessions. However, under present law coverage of the possessions would, as a practical matter, require the negotiation of mini-treaties, and the possessions to date have not clearly expressed interest in undertaking such an effort.

### C. Management of the Treaty Program

The questions of what U.S. tax treaty policy “is” and how it is formulated ultimately depend, of course, not only upon what the models or the treaties in force provide, or what view we take in the abstract about particular issues, but also upon our methods of conducting bilateral negotiations. This raises a host of questions about the “management” of the treaty program: how we formulate or revise provisions of the U.S. model; how we determine which countries we will negotiate with; how negotiations are actually conducted; and finally, how treaties in force are administered.

*Design of the U.S. model treaty.*—The most important decision that has been made in designing the U.S. model was to adhere as closely as possible to the OECD model. The discussion to this point indicates the basic justification for this approach: the OECD model represents an appropriate, if not perfect, theoretical basis for tax treaty negotiations; it evolved in a pragmatic way; and it offers the best chance of achieving the maximum degree of international tax harmonization, the reduction of tax-based barriers to the free movement of goods, persons, and capital across borders, with appropriate protections against international tax evasion. In light of the widespread international acceptance of the OECD model, any other choice would, in many cases, make the achievement of treaties impossible. These considerations have prevailed in the design of the U.S. model, despite the fact that much of the language used in that model is not found in the Internal Revenue Code; that some of the concepts of the OECD model are relatively unfamiliar as well; and that, in certain respects, we believe that substantive rules in the OECD model stand in need of improvement.

Those departures we have made from the OECD model are not generally motivated by differences in economic theory or differences in our view of the practical requirements of international tax cooperation. The only major exceptions to this statement are the reciprocal interest exemption and the investment and holding company provision. The interest exemption does reflect a consistent U.S. preference for a stricter “residence” basis approach to taxing liquid international capital which moves freely from country to country; but the approach we pursue is at least implicitly



conceded by the commentary to the OECD model. The investment and holding company provisions are, we believe, essential attributes of a modern bilateral treaty; but here again, the commentary acknowledges the validity of our position, and we are currently pursuing discussions at the OECD aimed at devising a common international view of treaty abuse. In general, if we believe a deviation from the OECD model is warranted based not on some peculiar circumstance of our position but because of deficiencies in the OECD approach, it is advisable to raise the question at the OECD, in an attempt to secure modification of the international model.

In general, most of the deviations we have made from the OECD model are an outgrowth of peculiar features of U.S. law. It is not necessarily true that our statutory practices in these regards are optimal, but treaties are intended to function against a backdrop of domestic law.

Finally, we are prepared to deviate from the OECD model in some instances in anticipation of changes in U.S. statutory law. Ordinarily, we would not deem it wise to change treaty policy in anticipation of statutory changes, because the changes might never occur. But we are conscious of the fact that treaties remain in effect for substantial periods of time, and are not subject to easy revision once they enter into force. Thus, when we perceive a likelihood that legislation will be enacted, and a difficulty with existing treaty policy if it is enacted, and when we view the potential legislation and the treaty policy changes as essentially sound, we are probably wisest to anticipate the legislation and modify our negotiating policy as appropriate.

*Selecting treaty partners.*—In cases where another country requests treaty negotiations with the United States, we are usually disposed—subject to scheduling constraints—to comply. Normally, we try to establish at the outset some of the ground rules under which we want negotiations to take place. For example, we forward a copy of the U.S. model in advance, sometimes accompanied by an explanation of its particular features; and we endeavor to make clear the U.S. position in regard to tax sparing and other incentives for foreign investment. Generally we indicate, in regard to treaties in existence, that we prefer not to negotiate exclusively for the purpose of changing a single provision. Existing treaties almost invariably stand in need of general updating, and if we are to meet we generally prefer a full review.

Insofar as U.S. initiated negotiations are concerned, it is best to distinguish between countries with which we already have a treaty and countries with which we seek a treaty for the first time. With respect to the former category, the most important instance where we might request negotiations would be where the treaty arrangement is producing unintended consequences. A leading example would be those treaties which give rise to extensive treaty shopping. Another case for U.S. initiated negotiations would be where significant changes in a treaty partner's law have undermined the functioning of the treaty or have altered the bargain represented by the treaty. An example would be our treaty arrangement with Italy, which has completely altered the tax system covered by the treaty in force.

A third case would be where a change in our own law has affected the operation of the treaty. Of necessity, we are slower in initiating renegotiation of treaties in this case, since changes in our law typically leave us with a host of treaties requiring revision. For example, the United States has not concertedly sought renegotiation of treaties to reflect changes brought about by the Foreign Investors Tax Act of 1966; over time, however, we have entered into negotiations because of other circumstances to revise at least half of those treaties; in these negotiations we have undertaken the necessary process of modernization. A systematic program to revise outdated treaties is on our agenda, but it does raise serious problems with the allocation of our staff resources.

A fourth case of U.S. initiated negotiations would be where Congress by statute overrode provisions of our treaties. This has occurred only rarely; the best known example was a provision of the Foreign Investors Tax Act of 1966 which overrode our estate tax treaty with Greece, which was then renegotiated. Congress is, however, now seriously considering adopting legislation to tax foreign investors on their capital gains from sales of U.S. real estate, and the pending legislation by its terms would override inconsistent treaty provisions after a 5-year delay. Our hope is that, in that 5-year period, we could negotiate protocols with the various countries with which we have treaties that would be subject to the override.

With respect to countries with which we have no treaties, we make it clear that we stand ready to negotiate but ordinarily do not urge any particular country to commence negotiations. We generally make the point that a tax treaty has substantial value, because it establishes fiscal relations between the two countries and because it represents an indication to private investors of the existence of a stable climate for investment. We normally do not press particular countries to negotiate, because it has been our experience that negotiations have the best chance for success where the other country comes on its own to recognize the desirability of a treaty relationship.

*The treaty bargaining process.*—In the process of bilateral bargaining, there are issues on which the U.S. and OECD models differ, where we are asked to make concessions in the direction of the OECD model; there are issues where we are asked to agree to a provision contrary to both models; and there are novel questions on which the models are silent.

With respect to movements in the direction of the OECD model, and movements away from both the U.S. and OECD models, there are some issues we never concede, and some where we must make a judgment based upon the overall balance of the treaty bargain. We do not concede, for example, on citizenship basis taxation; protecting provisions of U.S. law intended as penalties; noncoverage generally of state and local taxes; protection against at least some forms of discrimination; and the U.S. statutory rule regarding corporate residence. These are issues where we perceive a strong national interest reflected in the U.S. model. While we might make a concession on at least some of these issues in certain circumstances without serious impairment of our interests, we prefer not to establish precedents clearly contrary to the model on these questions. We believe each treaty represents a separate bargain, and do not make concessions simply because they have been granted in other negotiations. Nevertheless, in practice it is sometimes difficult to convince another country that we have good reason for not accepting a provision that we have accepted elsewhere.

On the other hand, there are provisions in the U.S. model which are different from those of the OECD model but to which we do not ascribe great significance. For example, the rules for resolving cases of dual residence of individuals are different in our model from those proposed by the OECD. We believe our rules are better than those of the OECD, but the differences are of little practical importance and we have been prepared to adopt the OECD rules.

Between these extremes lie a wide range of issues which must be considered on a treaty-by-treaty basis. The factors we normally take into account in making the necessary judgments are the practical importance of a concession to the United States and U.S. taxpayers; the provisions of foreign law that will be operative if the concession is made; the degree to which a particular concession might be regarded as a precedent for other negotiations; and the difficulties that a particular concession might create for the ratification process.

With respect to issues not covered by existing models, our objective in seeking agreement is frequently not conformity to principle but the establishment of a principle itself. Issues regarding the imputation credit are of particular difficulty precisely because what is involved for both countries is the establishment of a new principle. Eventually, of course, whatever principle is embodied in the treaties will, in some form, find its way into the work of international organizations, since that work has always been not so much a process of formulating abstract rules as of elaborating rules established, more or less, by usage. Because of the size and economic importance of the United States, we have special responsibilities in this regard; often when a new and serious international problem arises, like that created by the imputation systems, other countries will await the outcome of our negotiations before pursuing their own. These considerations can make bilateral negotiations over new issues very difficult.

Particular negotiations may raise special issues not covered, or not covered in sufficient detail, by the models. For example, discussions of information exchange with bank secrecy countries, and discussions of treaty shopping with tax havens, have made these negotiations unique. In these discussions we are not aiming at establishing or clarifying fiscal relations between two countries, but at solving a serious problem for the tax system. Just as we have fundamental concerns involved, the other country has concerns which it views as equally fundamental. In the best of circumstances the



"trade" made in such negotiations involves a compromise which improves the situation for both sides, without requiring ultimate concessions by either.

*Implementing tax treaties: the "competent authority" function.*—Under all tax treaties, certain powers and duties are delegated to the "competent authorities" of the contracting states. Under the U.S. model, and under our treaties in force, the term "competent authority" is the Secretary of the Treasury or his delegate; in practice, the Secretary has delegated this responsibility to the Commissioner of Internal Revenue, who in turn has delegated day-to-day responsibilities to the Assistant Commissioner (Compliance) of the Internal Revenue Service. On matters involving legal interpretations of treaties, the Assistant Commissioner (Compliance) is enjoined to seek the concurrence of the Assistant Commissioner (Technical).

The treaties spell out a number of assignments of the competent authority. The typical "mutual agreement" article states that a taxpayer may appeal to the competent authority of the state of which he is a resident or national, if he believes he is being subjected to taxation not in accordance with the treaty. The treaties authorize the competent authorities to agree to a definition of a term not defined in the treaty if an agreement on a common meaning is necessary or desirable. In addition, the treaties make the competent authorities responsible for conducting the information exchange permitted or required under the treaties. The competent authorities are authorized to communicate directly for the purpose of discharging their responsibilities. This provision is necessary to obviate using diplomatic channels to effect communication between the two contracting states.

One issue with respect to the implementation of our treaties grows out of the manner in which responsibilities for conducting the treaty program and implementing treaties are divided within the Treasury Department. The Internal Revenue Service is not, in general, responsible for the conduct of treaty negotiations; that function is reserved to the Treasury's Office of Tax Policy. Of necessity, however, the Service is assigned the task of handling the "competent authority" process. The most important reason for this is that the Service is in possession of the information which another country would be likely to request pursuant to a treaty, and knows what information the United States might need. In addition, the Service has the prime responsibility for handling individual tax cases.

*Public and congressional participation in the treaty-negotiating process.*—One final problem touching on the management of the treaty program concerns the difficulty of engaging Congress and the public in the process of formulating treaty law. Treaty negotiations are conducted on a government-to-government basis, and the provisions of a treaty are not revealed publicly until after a treaty is signed. This means that outside interested parties do not have a full opportunity to comment upon, or to participate in, the development of the provisions that will be included in the treaty; the treaty is presented as a fully negotiated document when it is transmitted by the President to the Senate for advice and consent.

We have taken several steps in recent years to mitigate this problem. In 1976 we published the U.S. model, calling for public comments. The model represents our initial negotiating position; through its publication we intended to apprise the public of our objectives in treaty negotiations, and we have, in fact, received significant comments on the model. Second, we have undertaken in recent years to announce publicly at least the outset of treaty negotiations; and as of 1978, for negotiations showing promise of leading to treaties, we have held public meetings to discuss the major issues and the negotiating positions of the United States. In order to do this, we must obtain the consent of our negotiating partner; and often we are constrained, at the request of other countries, in what we may publicly discuss. Most other countries with which we have negotiated treat the negotiating process as strictly secret. For this reason we have generally declined, in our public meetings, to divulge details regarding positions taken by the other country. Nevertheless, we do manage, through these meetings, to alert the public to most of the major issues in the negotiations, and we have frequently received useful comments and suggestions as a direct result.

Finally, the ratification process ensures full public participation after the signature of a treaty, but before it enters into force. If a provision is found objectionable to the Senate, there is ordinarily opportunity to reopen the negotiations to change the



provision, although this process may involve making collateral concessions to the treaty partner.

In general, it is difficult to see a way to avoid restrictions on public participation in the treaty negotiating process. Other countries typically insist upon some degree of confidentiality for the negotiations. Moreover, fully discussing our negotiating positions, the importance each has to us, our reasons for them, and the like would tend to undermine our own position in the negotiating process. This would have the effect of prolonging negotiations generally, and would inevitably result in less favorable bargains for the United States than we might otherwise be able to obtain.

### III. Conclusion

In summary, U.S. tax treaty policy is founded upon established international principles and practices, accommodated to reflect the special characteristics of our tax system. The essential long-range objectives of the tax treaty program are to eliminate the impediments that double taxation, or the threat of double taxation, might pose to the international flow of goods, capital, and persons, and to establish fiscal relations between the United States and other nations. In pursuing these objectives, we are sometimes forced to agree to compromise provisions that are not ideal, and to accept rules governing transactions with one country which may be different from those governing similar transactions with another. But if one considers the difficulties of making accommodations with the multitude of varying tax systems in the world today, the value of tax treaties to international economic activity clearly makes them worth these relatively small costs.

For the moment, the major short-term objectives of U.S. treaty policy are threefold: First, we must update and modernize our treaties presently in force. This process will eventually eliminate some of the irregularities of the extant pattern of treaty law. Second, we must revise those few treaties which give rise to abuse, for the sake of the integrity of the tax system and to ensure that the treaty program does not result in an unjustified loss of revenue to the United States. Finally, we need to work to expand our treaty network, particularly with developing countries. These objectives are serious and important, and they deserve a high priority; we are devoting to them as much time and effort as we can.

#### **Exhibit 50.—Statement of Secretary Miller, April 30, 1980, before the House Ways and Means Committee, on President's proposal for withholding on interest and dividends**

I am pleased to be here today to discuss the President's proposal for withholding on interest and dividends.

Underreporting of interest and dividend income is no longer a problem that we can afford to ignore. In 1979 taxpayers underreported interest and dividend income by about \$16 billion and thereby underpaid their taxes by approximately \$3.6 billion. Other taxpayers bear the cost of these lost revenues by paying a larger share of the tax burden.

Balancing the budget is a national priority in the fight against inflation. As we ask the American people to accept fiscal discipline, with cuts in spending for important economic and social programs, we must at the same time take positive action to avoid needless loss to the Treasury of billions of dollars due under present tax laws.

#### **Withholding is not a new tax.**

To combat this needless loss to the Treasury, the President has proposed a system of withholding on interest and dividends similar to the current system of withholding on the wages of our Nation's work force, a system that has served us well since 1943. Withholding benefits not only the Government, but also benefits taxpayers by providing them with a gradual and systematic way to pay their taxes.

Let me emphasize that withholding is not a new tax. As with wage withholding, withholding on interest and dividends does not increase anyone's tax liability; it only changes the method by which the taxes are paid. The purposes of the withholding program are simple: To collect taxes due on interest and dividend income, and to

ensure that all taxpayers report the full amount of their income and pay their fair share of taxes.

It has been strongly argued in recent years that the tax system relies too heavily on taxing savings and investment. This issue is being examined closely. But it cannot plausibly be argued that the way to lighten the tax burden on savings is to facilitate noncompliance with current tax laws.

### **Compliance is a current problem.**

Overall our system of income taxation works very smoothly. It is administered with honesty and integrity and with very low administrative and enforcement costs.

Nevertheless, a recent Internal Revenue Service report on income unreported by individuals clearly indicates that substantial numbers of individuals do not pay the full amount of tax that they owe because they fail to report the full amount of their investment income. The report presents the findings of a year-long study by an Internal Revenue Service task force appointed by the Commissioner to review all available data for the purpose of developing the best possible estimates of unreported income. The report determined that the 1976 gap between taxable interest payments received by individual taxpayers and taxable interest payments reported on individual income tax returns ranges from \$5.4 billion to \$9.4 billion. The 1976 gap between taxable dividend payments received by individuals and those reported on tax returns is estimated to range from \$2.1 billion to \$4.7 billion. While individuals are estimated to underreport wage income by only 2 to 3 percent, they omit 9 to 16 percent of interest and dividend income, a rate of noncompliance that is at least 300 percent greater.

As a result of continued substantial noncompliance in the reporting of investment income, about \$3.6 billion in taxes that were lawfully due were not collected in 1979. It is estimated that in calendar year 1981 this tax loss will increase to approximately \$3.9 billion.

Underreporting of investment income jeopardizes the very cornerstone of our tax system: self-assessment. The Internal Revenue Service now audits only about 2 percent of individual returns filed each year. Withholding provides a logical means to attain high compliance with low audit coverage.

### **Information reporting alone is not enough.**

Some have suggested that the existing system of information reporting—or an expanded system—would solve the reporting problem if only the Internal Revenue Service would do its job. In 1962 the Senate rejected the withholding approach adopted by the House on the ground that improved compliance should first be sought by expanding the information reporting requirements. This has been done.

The intervening 18 years have provided an ample test of information reporting alone as a compliance measure. The results of the recent Internal Revenue Service report on unreported income clearly indicate that, even with the additional reporting requirements enacted in the Revenue Act of 1962, taxpayers still fail to report and pay tax on significant amounts of taxable dividends and interest for which information reports are filed. Certainly the time has come to reassess how tax should be collected on interest and dividend income and why information reporting alone is not sufficient.

The Internal Revenue Service now matches at least 72 percent of the information documents that it receives on interest and dividends and uncovers several million discrepancies. Much of the nonreporting is apparently due to inadvertence, forgetfulness, and failure to keep records, particularly by taxpayers who receive relatively small amounts of dividend and interest income. Other nonreporting is due to nonfilers who owe some tax but who are difficult to trace. Because of the small amount of revenue to be gained from any one taxpayer, the cost of following up the millions of discrepancies is demonstrably uneconomical. Even extensive pursuit of taxpayers would not achieve full collection of unpaid taxes. There would be many unfruitful investigations where taxpayers cannot be reached by telephone or traced if they have moved. Even after the taxes have been assessed, it would be impossible or uneconomical to collect them.

The present situation, then, is that the Internal Revenue Service uncovers many more leads through its matching program than it pays to pursue. To follow up on all of

these leads would require millions of telephone calls, letters and visits, and audit efforts concentrated on individuals. This would inevitably be regarded as harassment of "little people" and would require shifts in staffing that would prevent the Service from directing its limited resources toward auditing compliance areas that are not susceptible to withholding.

### **Withholding is now necessary.**

How will withholding help? A substantial portion of the taxes that now go unpaid will be collected without costly audit procedures. Not only will withholding automatically collect much of the tax owed, but people will have more incentive to pay the remainder of their taxes due if part of their taxes have already been paid. The Service will be able to channel its audit resources to those areas where they are most needed and that best serve the public—the complicated returns of corporations, partnerships, and sophisticated high-bracket individuals.

The administration expects that withholding will also increase the accuracy of information being submitted to the Internal Revenue Service, thereby reducing the cost of reconciling discrepancies on returns. Since taxpayers will receive credit for withheld tax, they will have a positive incentive to supply payors with better information. Likewise, taxpayers will be less likely to lose or forget about their dividend and interest reports if these reports must be attached to the return in order to claim the credit. Information reporting alone provides no such incentives. The Internal Revenue Service estimates that more than 11 percent of information returns required to be filed by payors (Form 1099's) have inaccurate or missing social security numbers (taxpayer identification numbers), making accurate matching of documents in such cases extraordinarily expensive. By comparison, the rate of error on information returns for wages (form W-2), where the taxpayer is entitled to a credit for the taxes paid, is estimated to be about 3 percent.

Experience with wage withholding has proven that withholding is the most effective means of ensuring compliance in the reporting of income. Wage-earners now pay their taxes on a regular basis through withholding. Information reporting and the system of estimated tax payments simply have not been as effective. There is no reason why recipients of dividends and interest should not be held to the same standards of withholding and compliance that are set for wage-earners.

### **Summary of the proposal**

Under the President's proposal, 15 percent will be withheld on taxable dividends and interest paid to individuals with respect to deposits and securities of a type generally offered to the public. Most dividends and interest income is currently subject to information reporting; the proposal builds primarily upon the system that is now in place. The proposal also will extend withholding to instruments with respect to which reporting is not currently required, including obligations of the U.S. Government such as Treasury bills, as well as corporate coupon bonds and Government agency issues.

Payments to corporations (including corporate nominees and corporate trustees) and noncorporate securities dealers will be exempt from withholding. This exemption simplifies the withholding system administratively. Moreover, there are other safeguards to prevent noncompliance by these entities such as normally higher audit coverage by the Internal Revenue Service. Exempt recipients will include banks and thrift institutions, regulated investment companies, collective investment funds managed by banks, money market funds, and the like. All of these entities will, however, be required to withhold upon the payment of dividends or interest to their nonexempt customers, shareholders, or certificate holders.

Exempt organizations and individuals who reasonably believe they will owe no tax will not be subject to withholding if they file exemption certificates with the withholding agent. Furthermore, the proposal will be designed to minimize overwithholding and the period during which a taxpayer is owed a refund.

Under the proposal, it is estimated that tax collections for calendar year 1981 will increase by \$2.1 billion and \$2.3 and \$2.6 billion in 1982 and 1983, respectively.

A detailed description of the proposal will be provided in a separate technical explanation.



### **This proposal is different from the 1962 proposal.**

The President's proposal meets the objections that were raised to the proposal offered in 1962.

Although any withholding system will have complexities, the present proposal has been designed with simplicity and administrative ease in mind. Much of the complexity of the 1962 proposal stemmed from the level at which withholding was made. The present proposal designates as the withholding agent the entity that has the best information to determine the status of the recipient of the investment income. This approach, although more decentralized, makes exemptions easier to administer and more closely parallels the wage-withholding system.

Since 1962, the computer age has advanced us far along the road to solving administrative problems. As with the current information reporting system, taxpayers will receive reports showing the amount of investment income payable to them and the amount of tax withheld. They will not have to determine for themselves, as they would have in 1962, whether the amount of dividends and interest received was net of withholding or not.

Perhaps, in retrospect, installing a reporting system was the expedient approach in 1962. But in 1980, withholding is feasible and practical—as well as useful—in the effort to balance the budget.

### **Criticism of the proposal**

Despite the advantage of withholding, the proposal has been subject to some criticism. I would like to comment briefly on the main objections that have been raised.

*Cost to withholding agents.*—One objection is that withholding agents will incur additional administrative costs. Eighty-seven percent of the interest and dividends covered by the proposal is already subject to information reporting. For these, withholding agents need only add the amount of withheld tax to the reporting statement, remit the withheld tax to the Internal Revenue Service, and adjust the payments to the payee accordingly. Although withholding will be extended to instruments for which there is now no reporting, most of them are bearer securities held by corporations, and corporate recipients are exempt under the proposal.

Naturally there will be some start-up costs associated with adding withholding—there are always costs when an existing system is modified. But with a reporting system largely in place, we do not anticipate high continuing costs of the system to withholding agents.

The principal new cost will result from the exemption system. In recognition of this, exemption certificates will be permanent until they are revoked.

Overall, however, withholding is a far better way to collect taxes than is an increase in the number of audits, record checks, and collection attempts by the Internal Revenue Service. All taxpayers would bear the cost of increased audit coverage through the higher taxes needed to pay for the personnel and equipment necessary to conduct thorough examinations of more returns. Perhaps more importantly, taxpayers would suffer the loss of privacy from more frequent audits, record checks, and requests for detailed information. The success of the wage-withholding system indicates that taxpayers prefer withholding as a way to pay their taxes.

*Overwithholding.*—Some are worried that low-income taxpayers, particularly certain senior citizens who depend on interest and dividend income, will be overwithheld. The proposal will exempt individuals if they reasonably expect that they will owe no tax. This means that 70 percent of the senior population will be entirely exempt.

To deal with other problems of overwithholding and to contain the cost of instituting the withholding system within reasonable bounds, the Secretary will be given authority to provide additional individual exemptions by regulation. For example, the regulations could provide an exemption for married couples filing jointly who are at least age 65 and for whom, in both the prior year and the current year, interest and dividend income does not exceed a stated amount such as \$15,000, and total tax liability does not exceed 10 percent of their investment income.

Other individuals who incur tax liability will be able to reduce their estimated tax payments to take account of the tax withheld on their interest and dividends, including

interest and dividends that are eligible for the exclusion provided by the Crude Oil Windfall Profits Tax Act. Wage-earners will be able to adjust for tax withheld on interest and dividends that are eligible for the exclusion by reducing the amount of tax withheld from their wages.

Depository institutions will be permitted to withhold once at the end of the year on passbook accounts so that a taxpayer may apply for a refund shortly after the tax is withheld.

*Impact of savings.*—Withholding does not change savings incentives for individuals who now comply with the tax laws. Any argument that the tax system should encourage people to save by offering them opportunities to underreport their income must be rejected out-of-hand. Savings incentives in the form of opportunities for evasion promote inequity, undermine the integrity of the tax system, and are a grossly inefficient means of encouraging savings.

Some argue that the proposal will discourage savings by reducing the yield on savings. This argument confuses a change in the method of paying taxes such as through withholding, with a change in the overall level of taxation. If taxes are withheld, the amount withheld becomes a credit that taxpayers can claim against their final tax liability. Taxpayers may then adjust their estimated tax payments or simply reduce the balance due at the time that they file their returns.

Even if a taxpayer decides to make no adjustment during the year, he or she will only lose interest on the amount of tax that would not have been paid as early in the year if there were no withholding. Since the withheld tax on interest paid on a typical savings account averages less than one percent of asset value over the course of the year, at worst the "loss" of interest on the withheld tax would be less than one-tenth of 1 percent of asset value. Moreover, most of this loss will be avoided if withholding on passbook-type accounts occurs only at yearend, rather than quarterly.

Thus, the argument that savings will be adversely affected by this proposal is grossly overstated. Inflationary expectations and restricted yields on passbook savings have been the principal savings disincentives in recent years. Congress, with the full support of the administration, has already acted to lift interest ceilings through the phase-out of Regulation Q. Current economic problems should not lead us to advocate lower compliance with the tax laws as a policy for increasing savings.

## Conclusion

Withholding on wages proves that withholding is the most economical way to achieve high levels of compliance in the payment of taxes. The administration's proposal for withholding on interest and dividends will impose minimal burdens on withholding agents. It will also protect individuals with little or no tax liability.

Congress and the administration have at all times a joint responsibility to make certain that the Federal Government collects all taxes due it. In this period of fiscal austerity, we can ill afford the needless loss of billions of dollars in taxes that are not being paid on interest and dividends. Withholding on investment income is the most sensible and effective answer to this major compliance problem.

## Exhibit 51.—Statement of Deputy Assistant Secretary Sunley, August 5, 1980, before the Subcommittee on Taxation and Debt Management of the Senate Finance Committee, on the tax treatment of married and single taxpayers

The Treasury welcomes the opportunity to testify on the tax treatment of married couples and single individuals. This subject raises some of the most important issues in income tax policy and some of the most difficult to resolve. The Congress and the executive branch have wrestled with these issues since the establishment of the Federal income tax in 1913. The issues involve basic questions: Is the individual or the family the appropriate unit of taxation? Should the different circumstances of a family with one earner and a family with two earners be recognized? Should the special circumstance of a single person who maintains a household for children or other persons be recognized?

As it stands today, the tax law gives rise to tax increases and tax decreases when a marriage takes place and when a marriage is dissolved by reason of divorce or death. These tax consequences add to public concern about the fairness of the tax system. They also create concerns about the tax system's economic efficiency. For example, second earners among married couples and single persons are faced with greater work disincentives than are primary earners among married couples.

### Equity considerations

Tax policy has been guided by four important and widely accepted goals in the tax treatment of the family and single individuals.

First, *the income tax should be a progressive tax based on ability to pay*. The average tax rate should rise as income rises. A single individual with the same income as two individuals should pay more tax because that individual has more ability to pay. For example, more tax should be collected from a single person earning \$20,000 than should be collected from two single persons earning \$10,000 each.

Second, *married couples with equal combined income should pay the same tax*. No distinction should be made among married couples on the basis of how much of their combined income is earned by each spouse. For example, all married couples with total incomes of \$20,000 should pay the same tax, regardless of whether one spouse earns all of the income or each spouse earns half or differing portions.

Third, *a tax penalty should not be imposed on marriage*. Two single individuals should not pay a higher tax as a result of marriage. For example, a man and woman earning \$10,000 each should both pay the same tax whether they are married or single.

Fourth, *a tax penalty should not be imposed on becoming or staying single*. A single person should not pay more tax than another individual with equal income who is married to a spouse who has no earnings or income. Conversely, a couple should not pay higher taxes as a result of divorce. For example, a married couple with both spouses earning \$10,000 each should pay the same tax as two single persons both earning \$10,000.

While each of these goals is accepted as sound and fair, they conflict with one another. Any tax system will violate one or more of these goals. For example, if the second, third, and fourth goals are achieved in a tax system the tax cannot be progressive.

### 1. Historical development of current law

The history of the tax treatment of the family and single persons provides ample evidence of this conflict. The conflict is at the root of the issues under examination in present tax law.

a. *Rates*.—Between 1913 and 1948, the tax law recognized the individual as the unit of taxation. The tax system thus conformed with all the goals except the second, which requires the taxing of the combined incomes of the married couple. Consequently, couples with the same combined income had different tax liabilities.

Different treatment of couples with the same combined income was exacerbated by legal reallocation of property and income in "community property" States and by the ability of couples in other States to minimize taxes by reallocating property income. In 1948, the law was changed to allow the combining of incomes and income splitting; i.e., each spouse was presumed to have an equal amount of income whether or not that was the actual case. However, as a consequence of that decision, single taxpayers were required to pay more tax than most married couples with the same income. Looked at another way, a marriage bonus was introduced into the tax system in 1948.

The single penalty introduced in 1948 was most conspicuous in the case of single taxpayers with children—typically a widowed or divorced parent. In 1951, therefore, a special category of head of household was introduced. Tax rates for heads of household were set halfway between those of single persons and married couples. This was a compromise between the single individual's tax and the married couple's tax.

After 1948, there was a substantial tax increase for many earners who were made single due to the death of a spouse; for these taxpayers, the benefit of income splitting was immediately lost. Therefore, the law was changed in 1954 to allow a surviving spouse who maintains a household for a dependent child to continue to obtain the



benefits of income splitting for 2 years after the year of death of the spouse. After that period, the surviving spouse followed normal rules to determine whether he or she would file as a head of household or a single person.

A continuing concern about the single penalty (or the marriage bonus) led to enactment of lower rates for single persons effective in 1971. Since the rates for married couples were not changed, the benefit of income splitting was effectively eliminated at most income levels. A substantial marriage penalty was introduced; many two-earner families could pay lower taxes if they were single. To prevent two-earner married couples from taking advantage of the new single person rates, married couples were required to use the pre-1971 rate schedule for single persons if they filed separate returns.

The concern about the substantial marriage penalty introduced by the 1971 legislation led to a small reduction of the marriage penalty in 1979 when new rate schedules were introduced.

These actions since 1913 reflect decisions on the unit of taxation and the applicable tax rate schedules. The issue is even more complicated because of actions with respect to other Code provisions such as the standard deduction, the low-income allowance, the zero bracket amount, and the child care deduction and credit.

b. *Other Code provisions.*—Prior to the Tax Reduction Act of 1975, two single persons could claim two standard deductions or low-income allowances. If they married, however, they could claim only one. In the 1975 legislation, the low-income allowance and the maximum standard deduction allowed married taxpayers was made higher for married couples filing jointly than for single individuals. This reduced the marriage penalty but it also increased the single penalty. A single individual who married another individual with no income claimed a larger standard deduction than the amount claimed as a single individual.

In 1977, legislation repealed the standard deduction and introduced the zero bracket amount in all rate schedules. It provided that a certain amount of taxable income is subject to a tax rate of zero percent. The enactment of the zero bracket amount represented a compromise between reducing the marriage penalty and reducing the single penalty. The zero bracket amount currently is \$2,300 for a single person (and head of household) and \$3,400 for a married couple (and a surviving spouse). To the extent that a married two-earner couple has a smaller zero bracket (\$3,400) amount than twice the single earners' amount (\$4,600), there is a marriage penalty. To the extent that a married one-earner couple has a larger zero bracket amount (\$3,400) than that of a single person (\$2,300), there is a single penalty.

In all of these actions—defining the tax unit, prescribing appropriate rate schedules, providing zero bracket amounts—tax policy (since 1948) has accepted the first two goals—progressivity and the taxation of combined incomes of married couples—and has attempted to compromise the inconsistency between the marriage penalty and the single penalty.

As a result of these actions the Internal Revenue Code contains four different rate schedules for the individual income tax. Schedule X is used by almost 40 million single persons. Schedule Y (Part 1) is used by almost 46 million married couples filing joint returns (and surviving spouses). Schedule Y (Part 2) is used by 1.4 million married persons filing separate returns. Schedule Z is used by 6.3 million single persons who qualify as heads of households. Each schedule contains a zero bracket and positive rates ranging from 14 to 70 percent. (See table 1.)

Some limited recognition has also been given in past legislation to certain additional costs of earning income in the case of two-earners (and also a single person) who have children. In the 1954 legislation, a limited child care deduction was made available to married couples and single persons with incomes less than \$6,000. The deduction was expanded in both the 1971 and 1975 legislation, and in the 1976 legislation, the deduction was replaced with a credit equal to 20 percent of the first \$2,000 of child care expenses for one child and the first \$4,000 of such expenses for two children. The income limit also was removed. The child care credit can be viewed as a possible offset for the marriage penalty in the case of two-earner families with children. This is particularly true since the credit is not strictly limited to child care. The housekeeper often cleans the house and does the laundry. For a two-earner family without children

these same costs may be incurred in order for the second earner to enter the labor force, but the costs receive no special tax benefit under present law.

TABLE 1.—*Summary of the 1979 rate schedules*

Schedule in form 1040 instructions	Taxpayers covered	Number of returns using schedule in 1979 <sup>1</sup>	Amount of zero bracket in 1979
Schedule X.....	Single persons other than heads of households.	39.6 million	\$2,300
Schedule Y (part 1) .....	Joint returns of married couples, and certain surviving spouses.	45.7 million	3,400
Schedule Y (part 2) .....	Separate returns of married persons.	1.4 million	1,700
Schedule Z .....	Unmarried heads of households.	6.3 million	2,300

<sup>1</sup>Total individual returns: 93 million.

That is briefly the legislative history on attempts to resolve the issues. Let's look more specifically at present law and at the dimensions of the problem.

## 2. Present law

The current tax treatment reflects the progressive tax and generally taxes the combined income of husband and wife without distinction between one-earner and two-earner families, except for the child care credit. Both marriage penalties and single penalties exist in present law. Two wage earners who are married often pay more tax than they would if they were single. A single person often pays more tax than a married couple with the same income. The two-earner couple pays the same tax as the one-earner couple having the same total income. Except for the child care credit, the law ignores the additional costs incurred in earning income in the two-earner case.

a. *Marriage penalty.* —If two persons with independent incomes marry, they often have to pay a higher tax. For example, assume two persons each have taxable incomes of \$15,000 (after subtracting their exemptions) and assume they do not itemize their deductions. If they file as single individuals, they each must pay \$2,605 in tax. Their combined tax is therefore \$5,210. If they marry and file a joint return, their taxable income is \$30,000, and their tax (from schedule Y) is \$6,238. In this case, their marriage penalty is \$1,028. (See table 2 for examples of marriage penalties for selected levels of taxable income.)

However, it is not necessary that the two individual incomes be equal in order for a marriage penalty to arise. Suppose that the two persons have taxable incomes of \$22,000 and \$8,000, adding up to the same combined taxable income of \$30,000. Filing as single persons, their respective taxes are \$4,857 and \$977, for a total tax of \$5,834. If they marry and file jointly, their tax is \$6,238, for a marriage penalty of \$404. If the income is divided more unevenly, the marriage penalty will be smaller, or the couple may even save tax by marriage. Roughly speaking, the marriage penalty affects couples where the spouse with the lower earnings contributes at least 20 percent of the combined income.

TABLE 2.—*Married penalties in current law*

If two single people, each with taxable incomes* of—	marry, and have a combined taxable income* of—	their combined tax increases from—	to—	for a marriage penalty of—
\$5,000	\$10,000	\$844	\$1,062	\$218
10,000	20,000	2,774	3,225	451
15,000	30,000	5,210	6,238	1,028
20,000	40,000	8,354	10,226	1,872
30,000	60,000	15,924	19,678	3,754

\* "Taxable income" is total income minus exemptions of \$1,000 per person.

Married persons may file separately if they wish, but they must use the highest of the four rate schedules, and other special provisions occur throughout the Code to prevent them from saving tax in this way. As a consequence, the option for a married couple to file separate returns is not a defense against the marriage penalty.

b. *Single penalty.*—A single taxpayer often pays more tax than a married couple with the same income. For example, a single person with a taxable income of \$15,000 pays \$2,605 tax. But if a married couple has the same taxable income, even if it is all earned by one spouse, their tax is \$2,055. In this case, the single person pays 27 percent more tax. (See table 3 for examples of single penalties at selected levels of taxable income.)

These examples of the marriage and single penalties only take account of the differing rate schedules and zero bracket amounts. There are a large number of other provisions that impact on the tax treatment of married and single people. In some cases, single individuals and married couples filing jointly are subject to the same dollar limitations. Examples are the \$3,000 capital loss limitation and the maximum expenditures qualifying for the residential energy credit. In other cases such as the interest and dividend exclusion, the limitation for married couples filing jointly is twice that of single individuals. There are also cases where the limitation for married couples filing jointly are higher than that for single individuals but not twice as high. Examples include the maximum base and the beginning of the income phaseout for the credit for the elderly. Also, in order to claim the earned income credit, the credit for the elderly, and the disability income exclusion, married couples generally are required to file jointly. These credits are phased out based on combined income.

TABLE 3.—*Single penalties in current law*

If married couple with one earner and with taxable income* of—	divorces and the earner continues to have taxable income* of—	the earner's tax increases from—	to—	for a single penalty of—
\$5,000	\$5,000	\$224	\$422	\$198
10,000	10,000	1,062	1,387	325
15,000	15,000	2,055	2,605	550
20,000	20,000	3,225	4,177	952
30,000	30,000	6,238	7,962	1,724

\* "Taxable income" is total income minus exemptions of \$1,000 per person.

### Economic considerations

The current tax treatment of the second earners (or secondary investors) among married couples tends to distort decisions about labor market entry choices, about choices among occupations, about investment in education and training, and about investment in risk capital. This follows from the fact that second earners under the present system of combined income on joint returns face higher marginal tax rates than the rates faced by their spouses who are the primary earners or the rates faced by single persons. The argument can be made that the marginal tax rates of secondary earners—typically women—should be lower not higher than that of single women and married men. It is generally agreed that married women have substantial discretion over their labor market activity; i.e., they have a substantially higher elasticity of supply of labor than do single persons or married men. Thus, economic efficiency would be served if the marginal tax rates of secondary earners were lower than present rates. Economic efficiency in this sense means a reduction in the economic loss to society created by this distortion in labor force activity of married women.

### Dimensions of the problem

The marriage penalty and single penalty have become more serious issues as a result of increasing rates of divorce and cohabitation of unmarried couples, and the two-



earner married couple problem also has become a more serious issue as a result of increasing labor force participation by wives.

The most recent tax return data indicate that a marriage penalty is realized by a substantial number of couples filing joint tax returns. For tax year 1979, approximately 16 million will be affected by a marriage penalty totaling \$8.3 billion, while 24 million will experience a marriage bonus of \$19 billion.<sup>1</sup> (See table 4.)

TABLE 4.—*Distribution of marriage penalty and marriage bonus by income class under present law<sup>1</sup>*  
[1979 law, 1979 income levels]

Expanded income class	Marriage penalty			Marriage bonus		
	Number of returns	Amount	Average marriage penalty	Number of returns	Amount	Average marriage penalty
	(Thousands)	(Millions)		(Thousands)	(Millions)	
Less than \$10,000	655	\$83	\$124	4,120	\$1,063	\$258
\$10,000–\$15,000	2,058	437	212	3,940	1,439	365
\$15,000–\$20,000	3,207	908	283	3,650	1,809	496
\$20,000–\$30,000	6,416	2,350	366	6,196	4,632	748
\$30,000–\$50,000	2,867	2,465	860	4,412	5,755	1,304
\$50,000–\$100,000	527	1,179	2,235	1,297	3,303	2,548
\$100,000–\$200,000	123	494	4,018	185	764	4,127
\$200,000 and over	54	424	7,909	26	395	15,207
Total .....	15,906	8,340	524	23,827	19,160	804

<sup>1</sup> Dependent exemptions and deductible expenses are allocated to each spouse in proportion to each spouse's income and not in accordance with tax-minimizing behavior.

Labor force participation rates of wives of married couples since 1940 demonstrate the substantial growth of two-earner families. (See table 5.) The participation rate by wives increased more than 300 percent since 1940. The one-earner couple is no longer the predominant case. According to census data, in 1940 the one-earner couple accounted for almost two-thirds of all households. In 1978, the one-earner couple accounted for only about one-third.

### Basic options

The compromise between reducing the marriage penalty and the single penalty is always an uneasy one. The marriage penalty, in particular, has become one of the most widely criticized aspects of our income tax. But as long as the first two goals—progressivity and taxing combined income—are adhered to, the marriage penalty cannot be reduced without making the situation for single taxpayers even worse. If progressivity remains unchanged, any approach which alleviates both the marriage penalty and the single penalty must violate the combined income goal; i.e., there must be some differential in the tax law between one-earner and two-earner married couples.

TABLE 5.—*Labor force participation rates of wives of married couples, 1940–78*

Date	Participation rates	Date	Participation rates
	(Percent)		(Percent)
1940 .....	14.7	1973 .....	42.2
1950 .....	23.8	1974 .....	43.0
1960 .....	30.5	1975 .....	44.4
1970 .....	40.8	1976 .....	45.0
1971 .....	40.8	1977 .....	46.6
1972 .....	41.5	1978 .....	47.6

Source: U.S. Bureau of Labor Statistics.

<sup>1</sup> In making these estimates, it is assumed that exemptions and deductible expenses are allocated in proportion to each spouse's income. However, one spouse may itemize while the other spouse may use the zero bracket amount but the latter's deductible expenses are not assumed to be shifted to the itemizing spouse. Had it been assumed that each couple engages in tax minimization by allocating deductions, the number with a marriage penalty will be an estimated 18 million and the penalty will amount to an estimated \$13 billion at 1979 income levels.

Critics of the combined income goal argue that an economic difference justifies such a distinction: one-earner couples have the benefit of a full-time homemaker. Although the homemaker's services in the home are not measured in dollars, they do increase a couple's economic well-being and ability to pay. Two-earner couples do not have that advantage, and, arguably, this should result in a lower tax liability. According to a recent OECD survey, every industrialized nation with an income tax, except the United States, distinguishes between one-earner and two-earner couples, and even in the United States, the child care credit may be viewed as a distinction between one-earner couples without children and two-earner couples with children. It is one thing, of course, to support such a distinction and quite another to agree on what form it should take.

### **1. Abandon joint returns; require separate returns by married persons.**

One option is to abandon joint returns and income splitting and to require separate returns by married persons. This approach would also abandon head of household and surviving spouse statuses and abandon differential rate schedules for single persons and separate returns of married couples. Incidentally, most experts agree that Congress can require that each married person pay tax on his or her own income, determined without regard to State community property laws.

This option would eliminate both the marriage penalty and the single penalty. Only the combined income goal would be violated, as was the case in the pre-1948 income tax. The administrative convenience of joint returns could be retained by allowing married couples to file their separate returns on two parts of the same standard form, as is now done in some State income tax systems.

The option, however, has the potential for creating serious taxpayer compliance difficulties. The switch from joint returns to separate returns would effectively end the pooling of income and deductible expenses by married couples. Pooling of income and expenses has long served as a major simplification device. Under the options, each spouse would be taxed according to his or her own income and expenses. Each spouse would have to determine annually his and her proportion of ownership in jointly held income-producing property. Determining the share of ownership often would not be a one-time determination because spousal shares of ownership change as, for example, in the process of annual mortgage amortization, if one or the other spouse makes the payment. Special rules would be needed for trusts where one spouse receives the income from a property and the other spouse retains a reversionary interest in the property.

Assignment of income according to actual ownership could also create a real incentive to reduce tax by shifting ownership to spouse with the least income. It is noteworthy that some might view this as desirable on social policy grounds.

An alternative to assigning property income on the basis of ownership would be to use an arbitrary rule. One possibility would be to assign property income to the spouse with the most income. This might be considered unfair because property income would be taxed at higher marginal tax rates. There are, of course, many other possibilities for assignment of property income. Property income could be split on a 50/50 basis, even though this rule would treat property income more favorably than earned income.

As for assignment of earnings, it appears best to assign such income on the basis of actual earnings of the spouses, even though families engaged in closely held businesses and farms, could allocate earnings to a lower earning spouse rather arbitrarily.

The potential for arbitrary allocation of exemptions and deductions would also exist. One possibility would be to prorate the total amount of exemptions and deductions in accordance with the distribution of total income between the spouses.<sup>2</sup>

Another drawback of the mandatory option is its impact on tax burdens. Although the marriage and single penalties now created by differential rate schedules would be eliminated, tax burdens of individual taxpayers in terms of tax increases or tax decreases would depend on the rate schedule chosen. For example, if mandatory separate returns were required to use the current single person's rate schedule (and if heads of households and surviving spouses were also required to do so), almost all one-earner couples now receiving marriage bonuses, heads of households, and surviving spouses would have tax increases and some two-earner couples would have tax increases also. On the other hand, many two-earner families would have tax reductions. The tax increases in this approach would probably be unacceptable and other alternatives need to be considered.

To minimize the number of taxpayers who would have a tax increase, all taxpayers could be allowed the use of the most beneficial tax rate schedule in the law—that is the one for joint returns. Although the \$8.3 billion marriage penalty would be eliminated, the marriage bonus would be increased by \$9.7 billion. Single persons and heads of household would receive tax cuts of \$11.4 billion. The revenue cost of mandatory separate returns using the current joint return rate schedule would be \$29.5 billion at 1979 income levels. (See table 6.) The high revenue cost of mandatory separate returns is a serious drawback of this option.

## 2. Optional separate returns

A less costly alternative to mandatory separate returns would be to provide couples an option of filing jointly, as under present law, or filing separate returns as single persons. Heads of households and surviving spouses would continue to use their present rate schedules. The Mathias bill, S. 336, essentially follows this approach.

Although this option affectively eliminates the marriage penalty, it would not eliminate or reduce the marriage bonus (or single penalty). Under this approach, those benefiting from the marriage bonus (one-earner couples and two-earner couples with a low earner) would not be made worse off, except in a relative sense. They would generally continue to file joint returns to take advantage of the marriage bonus.

Optional separate returns has some of the same difficulties just noted with respect to mandatory separate returns, namely in the assignment of income and allocation of deductions. In addition, optional separate returns could seriously complicate taxpayer compliance since many couples would have to compute taxes two ways to determine which way minimizes taxes.

The revenue cost of optional separate returns treated as single persons would be \$8.3 billion at 1979 income levels. (See table 6.)

## 3. Return to full income splitting

Another option is to return to full income splitting, which was effective between 1948 and 1969. Under this approach, the joint rate schedule would have the same marginal tax rates as the single rate schedule in current law, but the bracket widths would be twice as wide. The zero bracket amounts for joint returns, separate returns, and single returns would remain as under present law. This option is philosophically the direct opposite of the mandatory or optional separate returns options discussed earlier. It retains the family as the basic unit of taxation rather than the individual. Each couple would continue to pool income and deductible expenses, would continue to divide their income equally for tax purposes irrespective of actual division of income, but would use single person's rates.

This option would eliminate the marriage penalty due to tax rates but not differing zero bracket amounts. It would recreate a sizable single penalty—up to 42 percent, compared with up to 20 percent under present law. The single penalty was extremely controversial in the pre-1969 era until reduced to 20 percent by the 1969 Tax Act. The option would also ignore the one-earner, two-earner couple issue; all pooled income

<sup>2</sup>It should be noted that the revenue estimates for this option and others which follow assume, where necessary, the 50/50 assignment rule for property income, the actual earnings rule for earned income, and the prorated allocation of exemptions and deductions according to total income.



TABLE 6.—Revenue effects of alternatives reducing marriage penalty and reduction in marriage penalty<sup>1</sup>  
[1979 law, 1979 levels]

Item	Mandatory separate returns; joint return rates for all taxpayers	Optional separate returns; single person rates (Mathias)	Two-earner couples: Deduction 10 % of first \$20,000 earnings of lowest earning spouse (Graval)	Return to full income split- ting using present single persons rates	Increases zero bracket amount for joint returns of \$4,600; for separate returns to \$2,300
<i>Billions</i>					
Current law marriage penalty .....	8.3	8.3	8.3	8.3	8.3
<hr/>					
Cost of alternative:					
Married couples:					
Reduction in marriage penalty .....	8.3	8.3	2.8	4.4	2.1
Increase in marriage bonus .....	9.7	—	0.7	10.4	3.2
Heads-of-house- holds .....	1.2	—	—	—	—
Single individ- uals .....	10.2	—	—	—	—
Total cost of alternative .....	29.5	8.3	3.5	14.8	5.4
<hr/>					
Remaining marriage penalty .....	0.0	0.0	5.6	4.0	6.2
Percentage reduc- tion in marriage penalty .....	100.0%	100.0%	34.0%	52.4%	25.7%

<sup>1</sup> Dependent exemptions and deductible expenses are allocated to each spouse in proportion to each spouse's income and not in accordance with tax minimizing behavior.

would continue to be taxed the same, irrespective of the actual division among spouses.

Although the option would reduce the \$8.3 billion marriage penalty by \$4.4 billion, it would substantially increase the single penalty (marriage bonus) by \$10.4 billion. The revenue cost of income splitting (based on present single rate schedule) would be \$14.8 billion at 1979 income levels. It would provide a substantial tax cut for marrieds. Although it would not actually create a tax increase for singles, it would increase relative tax between singles and married.

Recognizing that a single penalty of 42 percent is notably too high, it would be possible to reduce the progressivity of the marginal rate schedules (See table 7), have full income splitting and hold the single penalty to no more than 25 percent. An option along these lines, however, would cost \$23.3 billion at 1979 income levels, and even with such substantial tax reductions lower income single individuals would receive no tax reduction.

#### 4. Partial income splitting: Zero bracket amount for joint returns twice that of single person's

Another option would be to provide partial income splitting by increasing the \$3,400 zero bracket amount for joint returns to \$4,600, which would make it twice the amount now allowed single persons. Separate returns of married couples would have the same zero bracket amount, \$2,300, as that for single persons.

The effect of this approach would be in the same direction as option 3 but considerably more modest. The option would reduce the marriage penalty by \$2.1 billion mostly for lower income couples who do not itemize. (See table 8.) It would increase the single penalty (marriage bonus) by \$3.2 billion. The revenue cost would be \$5.4 billion. (See table 6).

TABLE 7.—*Marginal tax rate schedules for joint returns under present law and options to reduce the marriage penalty*

Taxable income bracket	Marginal tax rate on income in bracket		
	Present law	Tax rates designed to remove the marriage penalty <sup>1</sup>	
		With no reduction in single penalty <sup>2</sup>	With reduction in single penalty <sup>3</sup>
		Percent	
0- \$3,400 .....	0	0	0
\$3,400- \$5,500 .....	14	14	14
\$5,500- \$5,600 .....	16	14	14
\$5,600- \$7,600 .....	16	16	16
\$7,600- \$11,800 .....	18	18	18
\$11,800- \$11,900 .....	18	19	19
\$11,900- \$15,800 .....	21	19	19
\$15,800- \$16,000 .....	21	21	21
\$16,000- \$20,200 .....	24	21	21
\$20,200- \$20,400 .....	28	21	21
\$20,400- \$24,600 .....	28	24	24
\$24,600- \$28,800 .....	32	26	26
\$28,800- \$29,900 .....	32	30	28
\$29,900- \$35,200 .....	37	30	28
\$35,200- \$45,800 .....	43	34	30
\$45,800- \$56,400 .....	49	39	33
\$56,400- \$60,000 .....	49	44	35
\$60,000- \$67,000 .....	54	44	35
\$67,000- \$81,800 .....	54	49	37
\$81,800- \$85,600 .....	54	55	40
\$85,600- \$109,400 .....	59	55	40
\$109,400- \$162,400 .....	64	63	45
\$167,400- \$215,400 .....	68	68	51
\$215,400 and over .....	70	70	56

<sup>1</sup> Joint return schedule bracket widths double those of present law single return schedule for income taxed at positive rates.

<sup>2</sup> Present law single return rates used for joint and single returns results in a single penalty up to 42 percent.

<sup>3</sup> Reduced rates for joint and single returns results in a single penalty up to 25 percent.





## 5. Special deduction or exclusion on joint returns

If joint returns in their present form are preferred, it would still be possible to distinguish between one-earner and two-earner couples, by allowing a special deduction (or credit) based on the earnings of the second earner. It would be a simpler option in terms of compliance and administration than optional separate returns. A deduction from adjusted gross income of some portion of the lower earning spouse's income would be allowed. For example, the Gravel bill, S. 1247, would provide a 10-percent deduction up to \$20,000 of the spouse's earnings and the Sasser bill S. 1877, would provide a 20-percent deduction up to \$20,000 earnings. Depending on the deduction levels, this scheme would partially alleviate the marriage penalty. It would only give relief among two-earner couples. It would not alleviate any marriage penalty among two-earner couples resulting from investment income.

The drawback of this option is that some couples would receive tax relief in excess of their marriage penalty under present law. Therefore, an evaluation of this approach should include examination of how the total revenue loss should be allocated between reduction of the marriage penalty and increase of marriage bonus or single penalty.

Consider for illustrative purposes a deduction equal to 10 percent of the first \$20,000 of the lower earner's income. The revenue cost would be \$3.5 billion. (See table 6.) About 79 percent of the total cost would be allocated to reducing the marriage penalty and about 21 percent would be allocated to increasing the marriage bonus. The 10-percent deduction would eliminate about 34 percent of the marriage penalty under present law. It is noteworthy that the bulk of the lower earning spouses' incomes falls well below the assumed \$20,000 ceiling. Consequently, a higher ceiling above \$20,000 would have little effect either on the option's cost or on the reduction in the marriage penalty.

The number of returns experiencing a marriage penalty and the penalty amount would decline at each income level under this approach. (See table 9). Since the cost would also include tax relief in excess of the marriage penalty, it may be more equitable and less costly to target the tax relief more specifically at two-earner couples with a marriage penalty.

## Conclusion

In the process of developing a tax cut proposal, the administration will give serious consideration to the marriage penalty issue. The administration, however, is not making a recommendation at this time. A case can be made for each of the approaches. Some involve basic structural changes. Others are more simple corrective actions. The choice among them, of course, will depend on revenue considerations, acceptance of fundamental changes such as taxing the individual rather than the family, and tax simplification. These hearings provide an opportunity to gauge the views of interested groups.

TABLE 9.—Distribution of marriage penalty under present law and under two-earner option to deduct 10 percent of the first \$20,000 earned by lowest earning spouse by income class<sup>1</sup>  
[1979 law, 1979 income levels]

Expanded income class	Marriage penalty under present law			Marriage penalty remaining under the option		
	Number of returns	Average marriage penalty		Number of returns	Average marriage penalty	
	(Thousands)	(Millions)		(Thousands)	(Millions)	
Less than \$10,000 ..	655	\$83	\$124	\$561	\$65	\$116
\$10,000–\$15,000 .....	2,058	437	212	1,831	312	170
\$15,000–\$20,000 .....	3,207	908	282	2,584	589	228
\$20,000–\$30,000 .....	6,416	2,350	366	4,025	1,233	306
\$30,000–\$50,000 .....	2,867	2,465	860	2,034	1,489	732
\$50,000–\$100,000 ....	527	1,179	2,235	485	996	2,053

\$100,000–\$200,000 ..	123	494	4,018	120	461	3,839
\$200,000 and over ..	54	424	7,909	53	415	7,728
Total .....	15,906	8,340	524	11,692	5,560	476

<sup>1</sup> Dependent exemptions and deductible expenses are allocated to each spouse in proportion to each spouse's income and not in accordance with tax-minimizing behavior.

## Trade and Investment

### Exhibit 52.—Statement of Under Secretary Solomon, November 1, 1979, before the Subcommittee on Trade of the House Ways and Means Committee, in support of the trade agreement between the United States and the People's Republic of China

Mr. Chairman, the Treasury Department joins the other agencies here today in strongly supporting the trade agreement between the United States and the People's Republic of China. Under former Secretary Blumenthal's leadership, the Joint U.S.-China Economic Committee was established earlier this year to serve as a forum for the resolution of economic problems between our two nations and to help lay the foundation for the orderly development of economic and financial ties. This Committee, now under the chairmanship of Secretary Miller, will meet in 1980, hopefully in the early part of the year. This meeting will be the occasion for a visit to the United States by Chinese Vice Premier Yu Qiuli.

Treasury has also led the negotiations which produced the claims/assets agreement with China, an important first step toward normalization of our economic relations. As you know, the first Chinese payment under this agreement in the amount of \$30 million was made to the United States on October 1, and Treasury has just this week sent out vouchers to certified U.S. claimants. I will be glad to answer any questions you might have on this agreement.

The U.S.-China trade agreement represents an even more significant step in the overall development of our commercial and economic relationship with China. Rather than an obstacle from the past that had to be overcome—as with claims/assets—the trade agreement will look to the future, laying the foundation for the expansion of our trade and financial ties with significant long-term benefits for the American economy.

Since Secretary Kreps and Deputy Secretary Christopher have covered, respectively, the economic aspects and political context of this agreement—and Ambassador Askew will address the relationship between U.S.-China textile trade and the agreement—I will direct my remarks toward China's overall international economic position, including trade with other countries, external financing, and its external debt position.

China's total foreign two-way trade has increased sharply during the 1970's, from approximately \$6 billion in 1972 to more than \$20 billion in 1978, of which U.S.-China trade accounts for only a small part—roughly 6 percent in 1978. The sharp overall trade increase is due primarily to China's pursuit of a long-term modernization program which relies heavily on imported capital goods and technology. China's main trading partner during this period has been Japan, which currently accounts for approximately 25 percent of China's foreign trade, followed by Hong Kong with 11 percent, and Germany at 6 percent. Long-term trade agreements with the United Kingdom, France, Japan, Canada, and Italy should further boost China's foreign trade during the period ahead. China's trade with nonmarket economies constitutes only a relatively small part of its foreign trade—15 percent in 1978.

We expect China's foreign trade to continue to grow rapidly during the next few years. Imports for 1979 are expected to be in the range of \$15 billion, up from \$11 billion in 1978. By 1985, annual imports may be as large as \$40 billion.

The question arises as to how this trade will be financed. In the past, China's imports have been small, and limited by what foreign exchange China could earn through its exports. Imports of capital goods and services during the period immediately ahead will, however—because of China's modernization objectives—exceed its foreign exchange earnings capability. China will therefore need to finance a portion of its imports from foreign borrowing.

In light of this, China has sought both official and private lines of credit to meet its financing needs. Currently, both private and official credit lines totaling between \$23 billion and \$30 billion have been negotiated or are under discussion. Private credits—which account for about 20 to 30 percent of the total—are primarily syndicated Eurodollar loans, although there is some project financing by private investment groups.

The focus of China's effort to secure lines of credit, however, has been directed toward official government sources, and these represent the bulk of China's foreign credit lines. China has negotiated officially supported export credits with France for \$7 billion, Great Britain for \$5 billion, Canada for \$1.9 billion, and Italy for \$1 billion. Other export credit loans are now under discussion. In addition, Japan and China have agreed on an untied \$2 billion resource development loan, to be financed by Japan's Export-Import Bank, and, most recently, China has approached Japan for approximately \$3 1/2 billion in aid loans to finance nine development projects.

In order to avoid excessive official credit competition, official export loans offered China should meet the terms and conditions of the International Arrangement for Export Credits. It appears that most official creditors are conforming to the terms and spirit of the International Arrangement. The Japanese Eximbank credits, which have low interest rates, are not considered a derogation from the Arrangement due to the fact that they are not tied to Japanese exports. The Japanese Government has assured us that non-Japanese exporters will benefit from this financing. We would expect, therefore, that some of the Japanese financing will support U.S. exports.

The role of the United States in financing China's trade has, of course, been minimal. With regard to private financing, many foreign banks preceded their U.S. competitors into the China market. In the past year, however, the U.S. banking community has moved quickly into this market with over 30 U.S. banks establishing full U.S. correspondent relations with the Bank of China. We are aware of the negotiation of \$28 million in private credit lines between U.S. banks and China, and understand that additional credits are under discussion. In addition, we understand that the Bank of China, which currently has overseas branches in London, Singapore, Hong Kong, and Luxembourg, is preparing to open branches in New York and Tokyo in the not-too-distant future.

I have just noted the substantial official export credit which China has available from other nations. If U.S. exporters are to be competitive with foreign exporters—and establish a foothold in what could ultimately become an extremely important market for Western exports—then it is vital that the U.S. Government also provide appropriate export financing. As Deputy Secretary Christopher has mentioned, we are moving forward in this area. We are prepared to offer China competitive export financing from the Export-Import Bank so that U.S. firms are in a position to compete with foreign exporters in the China market. As you know, Vice President Mondale recently advised the Chinese that we are prepared to make available a credit arrangement up to a total of \$2 billion over a 5-year period on a case-by-case basis, and are willing to consider additional credit arrangements as developments warrant. The terms and conditions of these credits will, of course, be consistent with the International Arrangement on Export Credits. The approval of the agreement before you today is necessary for the extension of Eximbank financing—and therefore necessary to ensure that American exporters can compete effectively in the China market.

The use of balance of payments financing during the coming years will, of course, increase China's external debt. China has, however, historically taken a very prudent and cautious approach in its financial management. China's current debt service ratio is very low, approximately 6 percent. While this will undoubtedly rise somewhat, China to date has drawn very little on its new lines of credit, and we fully expect the Chinese to continue to take a careful approach to external financing.

In closing, I would like to reiterate that we view the trade agreement between China and the United States as a critical element in the normalization of our relations with China. I join my colleagues here today in strongly urging you to approve this agreement in order that we may lay the foundation for an expansion of our commercial and financial ties with China in a manner that is in the best interests of both nations.



**Exhibit 53.—Press release, December 20, 1979, entitled “Treasury Announces Contract for Solar Electric System”**

The Solar Energy Research Institute today signed on behalf of the U.S.-Saudi Arabian joint solar energy program a \$16.4 million contract with the Martin-Marietta Corporation to design and construct the world's largest solar powered photovoltaic electrical system. The 350 kilowatt photovoltaic system will be located between two villages about 30 miles northwest of Riyadh, the capital of Saudi Arabia.

This jointly funded project is the first of several to be initiated in the field of solar energy research under the United States-Saudi Arabian Joint Commission on Economic Cooperation. Other projects under this cooperative effort will be carried out in the United States as well as Saudi Arabia.

The U.S. Departments of Energy and Treasury and the Saudi Arabian National Center for Science and Technology and the Ministry of Finance and National Economy are parties to the five-year, \$100 million agreement. Each government will make matching contributions of \$50 million over the life of the program.

The photovoltaic system is to be in operation by June 1981.

The Secretary of the Treasury G. William Miller and the Minister of Finance Muhammad Abalkhail serve as the co-chairmen of the Joint Commission. The SERI serves as the operating agent for the solar energy program.

**Exhibit 54.—Excerpts from remarks by Assistant Secretary Bergsten, February 28, 1980, before the American Law Institute/American Bar Association, New York, N.Y., entitled “Toward Greater Cooperation in International Investment Policies”**

More than ever before, investment has become an engine of future economic growth and a key factor influencing future trade flows. Increased domestic investment has become a common objective of all nations, including the United States. We need more investment to support more jobs, more exports, more productive capacity to fight inflation, and new technologies.

Investment across national borders can be a major contributor to achieving these objectives. The United States has, therefore, traditionally supported and currently maintains an open policy toward both outward and inward private investment.

In promoting these objectives, however, governments at both federal and subfederal levels frequently adopt measures which can distort the allocation of investment among nations, reduce the potential gains from international specialization, and prompt countermeasures by other governments. Key problems involve the use of financial, trade, tax, and other incentives to attract foreign investment which might otherwise locate elsewhere, and the imposition of performance requirements which seek to tilt the economic benefits stemming from particular investments to one country at the expense of others.

However, there is at present virtually no international regulation of government actions in the investment field—no guidelines for what is acceptable, no recognized recourse against harmful actions by others. The problems resulting from government interference in this area are proliferating, and will become even more troublesome in the decade ahead. Improved international cooperation is essential.

Today I would like to discuss some of the most important problems we face concerning international investment, the progress we have achieved so far in enhancing cooperation, and some ideas about further steps in this key area.

\* \* \* \* \*

**Need for cooperation**

A major objective of U.S. policy during the past 3 years has therefore been to achieve increased multilateral discipline on incentives and other interventions by governments, both to maintain an open investment environment and to avoid emulative countermeasures. The 1976 OECD Declaration on International Investment and Multinational Enterprises deals with aspects of the problem. Although limited in its scope and impact, it represents a significant first step in creating multilateral

agreement and increasing international cooperation on investment issues. Bilateral investment treaties and treaties of friendship, commerce, and navigation deal with some aspects of the investment relationship. None of these, however, constitutes more than a start at achieving international cooperation in this area.

We now have an international code governing the use of subsidies and countervailing duties—one of the most important accomplishments of the recent round of multilateral trade negotiations. We do not have a code for investment incentives or performance requirements. We should. Even more basic, but more long term in nature, we should have a “GATT for investment” similar to the GATT we now have for trade: A common body of rights and regulations which defines acceptable actions and provides recourse for those whose rights are harmed. Such an arrangement would not necessarily embody a single international institution, like the GATT for trade—but it should embody rules of the game and institutional arrangements which would serve as a functional equivalent.

\* \* \* \* \*

### A “GATT for investment”

It is impossible to predict the form that international cooperation in the investment area might ultimately take. I use the term “GATT for investment” to convey the concept of an overall body of rules and institutional arrangements to govern international investment. The term does not necessarily mean a new institution solely for investment purposes. It could well be a series of arrangements grafted onto existing international bodies.

Such a “GATT for investment” need not be elaborate or comprehensive in its initial stages. It could build upon the progress already underway and evolve gradually into a comprehensive set of international regulations governing investment actions. It would not happen overnight, but would reflect a common recognition of the need for cooperation and embody a series of individual steps, taken both multilaterally and bilaterally, toward this common objective.

Initial first steps toward a “GATT for investment” could include agreement in the following areas: (1) Transparency of current investment measures; (2) notification of any future measures which might be adopted; (3) a standstill on current measures or levels of measures; and (4) over time, a rollback of existing investment measures.

Similar commitments provided the original basis for the development of the GATT for trade—an agreement which has evolved into a widely accepted set of international rights and obligations, a formal organization for discussion of common problems, and specific dispute resolution procedures. The basic framework of the GATT has been revised and expanded to meet the needs of today’s rapidly changing world economy through the recent multilateral trade negotiations. Members now include more than 80 nations which account for over three-fourths of world trade.

### Other models

Besides the GATT for trade, there are a number of other models to consider as building blocks. Two of the most important are the new code on subsidies and countervailing measures, and the European Community’s internal experience in regulating investment incentives.

The subsidies code provides an immediate basis for getting at some investment incentives and performance requirements which can cause injury to other nations. It incorporates the triple requirements of transparency, notification, and consultation.

Domestic subsidies are explicitly recognized as countervailable subsidies under the new code, provided injury is shown. Nations agree to seek to avoid causing serious prejudice to other nations in using subsidies to eliminate industrial, economic, and social disadvantages in specific regions, to facilitate the restructuring of certain sectors, to sustain employment and encourage retraining and change in employment, or to encourage research and development programs. They also agree to consider possible adverse effects of such measures on trade and existing conditions of world trade, production, and supply in the product concerned. Examples of general kinds of subsidies understood to be covered by the code include government financing of

commercial enterprises, including grants, loans, or guarantees; government provision or government-financed provision of utility, supply distribution, and other operational or support services or facilities; government financing of research and development programs; fiscal incentives; and government subscription to, or provision of, equity capital.

Nations also have the right to retaliate against domestic subsidies which impair GATT tariff bindings for which reciprocal concessions have been negotiated. Such subsidies become an alternative to tariff protection to restrict access to domestic markets.

Within the broad category of subsidies is a specific set of practices classified as "export subsidies." Signatories commit themselves not to grant export subsidies on products other than certain primary products. The "export subsidy" concept singles out those subsidy practices which differentiate between sales destined for domestic markets and sales destined for export markets. Prohibited export subsidies specifically include the provision by governments of direct subsidies to a firm or industry contingent upon export performance.

These rules, however, are effective only after trade begins to flow and injury can be shown. Trade sanctions, such as countervailing duties, have traditionally been taken after production is underway and trade is established, long after millions of dollars are invested in a facility and jobs are transferred from one location to another. When that kind of damage has already been done, the usefulness of trade sanctions as a remedy for the injury is quite limited.

A major objective in the investment area would be to move the coverage of international discipline back from the point at which trade flows to the actual investment decision, and to apply it to potential distortions on the import as well as the export side.

The second key model is the European Community's system of rules which places a limit on the investment aids granted by the member countries to assure that there will be no distortion of competition in the production of goods within the Community as a whole. The rules have evolved gradually on a selective basis but now provide for a general surveillance role for the EC Commission. The Commission's authority extends in particular to (1) regional aids designed to offset special handicaps (i.e., low standard of living, serious unemployment) or to facilitate the development of certain economic areas; and (2) sectoral aids designed to facilitate the development or restructuring of certain industries or to promote an important project of common EC interest.

The Commission's powers involve regular review, a requirement for prenotification of new projects or changes in current projects, a right to initiate an examination or require information to be supplied by member countries to make sure that the agreed limits on investment incentives have not been exceeded, and the power to rule that proposed aids are incompatible with the Treaty of Rome. Member countries that do not comply with Commission decisions may be taken to the EC Court of Justice. The EC experience has demonstrated the importance of transparency—or measurability—in member-country investment aids and the need to distinguish between aids which distort competition in an adverse manner and those which are beneficial.

Would it be possible to generalize the EC rules, at least to the OECD nations? Could the OECD be an institutional reference point similar to the EC Commission within the Community? Is this a path we might want to pursue?

It is no accident that investment rules have developed most fully where free trade exists, as within the European Community. Once nations have ruled out the use of trade barriers among themselves, governments are increasingly tempted to influence trade flows via investment policies. Investment rules are necessary, therefore, to restrict the use of investment distortions, and thereby complement and maintain the benefits of the open trade arrangement.

### Defining acceptable measures

In designing a "GATT for investment," we will also have to devise a basis for defining acceptable and unacceptable investment measures. In the incentive area, we might ask:



- When is an incentive legitimate as a means to offset the disadvantage of investing in a particular locale, and when does it exceed that bound?
- When does an incentive actually induce a firm to shift production from one nation to another, as opposed to influencing where among several sites within a nation it might locate?

We do not have clear answers to these questions. However, two principles can be tentatively put forth: An undesirable investment incentive would be one which would both (1) cause industrial investment to be located in the territory of the nation granting the incentive, while in the absence of the incentive the investment would go to some other nation's territory; and (2) distort the efficient allocation of resources as between any pair of nations.

It should be noted that, under these principles, measures which are sometimes referred to as "incentives" but in fact amount to the removal of government-imposed disincentives to investment would not be condemned. Such exempt measures, for example, would include broad-based tax reductions and the liberalization of government regulations which affect business. These measures would constitute a move by government toward a "neutral" role in investment decisions. If one government moves toward "neutrality," it should be above criticism by other governments. By contrast, direct or indirect subsidies to a firm which are not compensatory in nature—including operating subsidies, subsidized loans, free provision or payment of front-end cash or noncash grants to the firm—would be covered.

Two categories of incentives may require special treatment. One encompasses incentives designed to draw investment into disadvantaged or depressed regions of a nation. The other covers incentives to research and development. Arguments based on sound economic reasoning suggest that a limited case might be made for direct subsidies in each of these areas. Even here, however, limits on the use of such incentives are necessary, as EC experience has shown. Maximum subsidies in the European Community for aid to depressed regions generally have been limited to 20 percent of the total project.

Dealing with performance requirements is at least as difficult as dealing with investment incentives. In general terms, it can be argued on economic grounds that any performance requirement is undesirable unless it acts to offset some imperfection in the working of the market.

The problem is to determine what, if any, imperfections exist in a given situation and to determine if performance requirements act solely to correct the deficiency. Such a determination is particularly thorny in the case of some developing countries. Performance requirements are often justified as necessary to offset the alleged market power of multinational enterprises and thereby assure that they meet the goals of host governments. But abuses by multinational firms in developing nations are exaggerated, and we believe that the case for performance requirements is vastly overstated.

### Coverage of States, localities

A lesson which a number of nations are increasingly recognizing is that all levels of government need to be involved in this cooperative effort, including the U.S. States, the Canadian provinces, and the German *laender*. Indeed, many of our States are already uneasy over the competition among themselves for new investments—a process quite similar to the international situation I have been describing. During one discussion of this topic, a State development official commented that "we wasted \$5 billion last year in subsidizing private firms."

The United States cannot afford, at either the Federal or State levels of government, to ignore the effects of State actions on American economic relations with other countries. In the past, a foreign firm usually made a strategic decision to invest in the United States; then it searched for a suitable location, often shopping between anxious States for the best bid. While this two-stage process was expensive for the bidding States, it did not create international difficulties. But with the increasing internationalization of production, foreign countries have frequently become attractive alternatives for servicing the American market. The States, therefore, now often find themselves competing with foreign governments—as well as with each other—in bidding for an individual plant.

\* \* \* \* \*

In other areas where progress has been achieved in curbing or studying Federal practices, State and local practices are either explicitly or implicitly included. The OECD medium-term study of investment incentives and disincentives will cover the practices of all levels of government: local, state, and national. The United States intends to use the new subsidy code's provisions in its efforts to limit the subsidy practices of foreign governments at both federal and subfederal levels. Other signatories can be expected to do the same with regard to American subsidy practices.

Under these and other agreements, subfederal units will be affected to varying degrees. Under some agreements, the States do not have formal obligations but their economic policies may be subject to foreign retaliation. Under other agreements, a direct challenge to State policies may be mounted in the U.S. courts. In any event, both the State and Federal governments will be involved in the notification, consultation, and dispute settlement phases of these problems.

### Conclusion

The United States has a basic national interest in seeking improved international cooperation in the investment field.

As a home country for U.S. industries, we don't want to see our industries lured abroad by foreign incentives that deprive the U.S. economy of jobs, income, and export earnings. Performance requirements imposed on U.S. firms investing abroad can also decrease exports from the United States, and increase sales back to our market.

As a host country to foreign investment, we are concerned about the dual problems of competition for investment among our own States and assuring that foreign investment which would benefit U.S. jobs and industrial production isn't lured elsewhere.

Investment is an essential determinant of economic growth and a key element in trade flows. Cooperation in this area is as important as in trade and monetary affairs. We are encouraged that progress is being made. We will continue to work for more progress in the future.

**Exhibit 55.—Excerpts from remarks by Assistant Secretary Bergsten, March 18, 1980, before the American-Arab Association for Commerce and Industry, New York, N.Y., entitled "United States-Saudi Economic Interests"**

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There are many important aspects to the United States-Saudi relationship. Energy and finance are key elements, with considerable impact not only on our own economies but on the entire world. Trade in nonenergy products is becoming increasingly important, as well. The United States-Saudi Joint Economic Commission offers a third facet of our economic relations which is important to Saudi economic development and our continued close cooperation in the future.

\* \* \* \* \*

The Commission has been in existence for almost 6 years. \*\*\* The joint statement issued by Crown Prince Fahd and former Secretary of State Kissinger in 1974 expressed the mutual desire of Saudi Arabia and the United States to work together to "promote programs of industrialization, trade, manpower training, agriculture, and science and technology." Since that time, the Joint Commission has become an active mechanism to bring together the expertise of various parts of the United States and Saudi Arabian Governments and their respective private sectors to pursue Saudi development goals.

Structurally, the Joint Commission has a system of parallel direction in which Secretary of the Treasury Miller and Minister of Finance and National Economy Mohammed Abalkhair serve as cochairmen, \*\*\*.

In order to support and coordinate Joint Commission work on the U.S. side, the Treasury Department established an Office of Saudi Arabian Affairs in Washington, and later an office of the U.S. Representation to the Joint Commission in Riyadh.

Technical cooperation programs under the Joint Commission are provided by the United States to the Saudi Arabian Government on a cost-reimbursable basis in accordance with a technical cooperation agreement initially signed early in 1975. During Secretary Miller's visit to Riyadh last November, this agreement was formally extended for another 5-year period. Projects are financed by drawing against a Saudi Arabian trust account which is held by the U.S. Treasury Department. U.S. specialists work side-by-side with Saudi counterparts on a multiyear basis in the various ministries and agencies. More than 150 of these specialists are now in Saudi Arabia.

To date, agreement has been reached on 20 major projects which cover a broad range of economic activities and which have a total ultimate value in excess of \$750 million. Projects are being carried out in areas as diverse as vocational training and highway transportation. They share a common goal: The expansion of the Saudi Government's capability to plan, guide, and monitor its development effort.

\* \* \* three project areas which offer major developmental benefits to Saudi Arabia: An electrification plan, cooperation in solar power development, and the building of vocational training centers through the Kingdom.

### Powergrid project

One of the most significant tasks we have been asked by the Saudis to undertake, under the auspices of the Joint Commission, is the development of an electrification plan for the Kingdom which will cover the next 25 years. \* \* \*.

\* \* \* \* \*

\* \* \* The plan calls for a nearly fortyfold increase in the generating capacity of the Saudi power industry. Demand is increasing at a rate of about 25 percent a year, compared to an annual increase of about 5 percent in the United States since 1973. The capital cost for the new generating, transmission, and distribution facilities over the life of the plan will be over \$70 billion when figured with a 7-percent annual inflation rate. Such an incredible expenditure will provide the Saudis with an electrification system about equal to what we enjoy in this country today.

### Soleras

A second major program involves United States-Saudi cooperation for solar energy development. This unique agreement is a jointly funded program under the auspices of the Joint Commission. Over the next 5 years, both the United States and Saudi Arabia will provide \$50 million to the \$100 million program agreement.

The first projects will include the design and installation of the world's largest solar photovoltaic electrical system for two existing villages about 50 kilometers from Riyadh. \* \* \*.

In time, this \$12 million solar village project could serve as the prototype for rural electric development in Saudi Arabia and other developing countries. \* \* \*.

Other projects expected to be initiated under the solar agreement this year include an engineering test of a large Sun-powered air conditioner mounted on a commercial building in the United States. We also are planning projects to study the socioeconomic effects of the solar system on the two villages and the establishment of solar insulation measuring stations at several sites in Saudi Arabia. Discussion will begin soon also for the testing of solar air conditioners in Saudi Arabia, and the design and construction in the United States of a solar desalination device.

\* \* \* \* \*

The VOTRAKON (vocational training) project is designed to increase both the number and skills of Saudi craftsmen through systematic strengthening of vocational training curricula and construction of additional training facilities. Work is well underway in the areas of machine shop trades, automotive repair, welding, diesel engine repair, air conditioning repair and refrigeration, electricity, and plumbing. Saudi Arabians will be trained in developing and using instructional materials incorporating the most modern techniques and equipment. High priority is also being given to building an effective on-the-job training program throughout the Kingdom.



\* \* \* \* \*

To expand the capacity of the Ministry's vocational training system, the U.S. Department of Labor and the General Services Administration are heavily involved in the design and construction of the new Instructor Training Institute as well as 10 new training facilities and housing for both students and instructors at 15 existing training sites.

As part of the overall project effort, a competitive plan is being prepared to expand an existing effort in the United States for preparing Saudi administrators and instructors for their jobs in the new training system. It is estimated that over 300 Saudi personnel may be trained here in the United States as part of this project.

\* \* \* \* \*

**Exhibit 56.—Excerpts from Joint Communique of the Fifth Session of the United States-Saudi Arabian Joint Commission on Economic Cooperation, April 1-2, 1980, Washington, D.C.**

The United States-Saudi Arabian Joint Commission on Economic Cooperation met for its Fifth Formal Session in Washington, D.C., April 1-2, 1980. The Secretary of the Treasury of the United States, the Honorable G. William Miller, chaired the meeting. The Minister of Finance and National Economy of the Kingdom of Saudi Arabia, His Excellency Muhammed Al-Ali Abalkhail, Co-Chairman of the Joint Commission, led the Saudi Arabian delegation.

\* \* \* \* \*

The two delegations noted with satisfaction the extension of the Technical Cooperation Agreement which provides the framework for the operations of the Joint Commission. The extension was signed on November 25, 1979, by the Co-Chairmen during Secretary Miller's visit to Saudi Arabia, and will be the basis for continued Commission activity until February 13, 1985.

Pursuant to the terms of the Extension Agreement, the Commission reviewed the status and progress of cooperative projects carried out under the auspices of the Commission and discussed new areas of cooperation between the two countries. The discussions made clear the high priority both governments place on the bilateral technical cooperation under the Joint Commission and the significant contribution the program makes to strengthening the ties between the two countries.

In considering the future work of the Commission, the Saudi delegation drew attention to the contribution the Commission's programs make to meeting the goals of Saudi Arabia's third Five-Year Development Plan to begin in mid-1980.

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In addition to the plenary sessions, special bilateral working groups met to review in detail the cooperative projects in the various fields of Joint Commission activity, with particular emphasis on recently expanded and new projects in agriculture and water, desalination, agricultural credit, manpower training and development, science and technology research, highway administration, and consumer protection.

\* \* \* \* \*

**Overall assessment**

The Fifth Session of the Commission proved to be most valuable since it combined useful plenary sessions with a series of technical meetings of bilateral working groups. This new approach was welcomed by the two delegations since it permitted more detailed reviews of the Joint Commission programs, and fostered closer working relationships between the Saudi and U.S. Government officials.

The Commission expressed its thanks to all the participating Saudi Arabian ministries and American departments and agencies for their fine spirit of cooperation. It was agreed that both sides will continue to explore possible new areas of technical cooperation.

In concluding its 1980 session, the Joint Commission approved the issuance of an Annual Report which outlines the purpose of the Commission and its development

during the past five years, and provides detailed information regarding the various projects.

\* \* \* \* \*

The Co-Chairmen agreed to hold the next Joint Commission meeting in the Kingdom of Saudi Arabia in 1981.

**Exhibit 57.—Excerpts from statement by Assistant Secretary Bergsten, May 22, 1980, before the Subcommittee on International Finance of the Senate Committee on Banking, Housing, and Urban Affairs, on the Competitive Export Financing Act of 1980 (S. 2339) and the Export Expansion Facilities Amendments of 1980 (S. 2340)**

Thank you, Mr. Chairman, for this opportunity to testify on the Competitive Export Financing Act of 1980 (S. 2339) and the Export Expansion Facilities Amendments of 1980 (S. 2340). The goal of the first bill is to discourage the use of predatory export financing measures by other countries. The goal of the second bill is to prompt the U.S. Export-Import Bank to finance projects that the private capital market would not necessarily support at rates competitive with foreign financing.

The longstanding goal of our efforts in the export credits field, as you know, has been to reduce and eliminate subsidies. These subsidies are not small. Mr. Axel Wallen, the Chairman of the OECD's Export Credits Group, has estimated that the Participants in the Arrangement on Guidelines for Officially Supported Export Credits—the industrialized OECD countries—may provide between 3 and 5 billion dollars in export credit subsidies this year.

To achieve our goals, we have developed and implemented a two-track strategy. The first track is intensive negotiations to limit subsidies multilaterally. The second track is a more aggressive Eximbank, to indicate clearly that the United States will not permit its exporters to be rendered uncompetitive as a result of the export credit practices of other countries.

**International negotiations—the first track**

On the first track, we have pressed increasingly hard for meaningful international negotiations. In the past 3 years alone, we have had 31 bilateral and multilateral talks with Arrangement Participants. These negotiations have been even more intense than the celebrated subsidy code talks in the multilateral trade negotiations. \* \* \*

\* \* \* \* \*

In March 1979, President Carter reported to Congress on the state of the negotiations to improve the Arrangement. He noted that the unanimity required to increase the Arrangement interest rate structure was lacking, and that, as a result, we would modify Eximbank's programs to be more aggressive. The President added that we would press ahead with negotiations when other countries showed more willingness to achieve a greater measure of international discipline.

Last fall, other countries showed a willingness to try again and a new round of negotiations began. The most important result so far is the Wallen Report, named after its principal author. The report proposed an entirely new framework for official export credits.

**The new framework**

There are two basic problems with the existing Arrangement. First, its interest rate minimums are fixed; fluctuations in market interest rates, particularly in an upward direction, can thus produce sharp divergences between Arrangement and market conditions and generate major increases in subsidy levels. Second, its interest rates are identical for all currencies. However, market rates differ sharply from country to country (as well as over time, for all countries) and thus create anomalies among countries with major competitive implications.

The new framework proposed in the Wallen Report involves a differentiated rate system for export credits, which would rectify both problems: It would vary the

minimum interest rates on official export credits by currency, and it would synchronize these minimum interest rates with actual rates in the respective capital markets.

The idea would be to have a different interest rate minimum for each lending currency. The market rates of interest on loans in the currency of a country with a low rate of inflation tend to be lower than for loans in the currency of a country with a high rate of inflation. However, the minimum rates of interest are the same for all currencies under the present Arrangement on Export Credits. Thus a high inflation rate country can subsidize exports as compared to a low inflation rate country and still comply with the Arrangement Guidelines. The new framework would eliminate this competitive inequity.

Second, the proposed new framework would not only relate the minimum interest rates to market rates of interest in the various major currencies, it would change these rates from time to time as capital market rates change. The idea would be to adjust the minimum interest rates, periodically and automatically, using long-term government bond yields in the various countries as benchmarks. This would avoid the built-in delays we face at present in trying, by negotiation, to adjust Arrangement interest rates.

\* \* \* \* \*

The U.S. Government firmly supports a differentiated rate system. Such a system would place all official export credit offers on a much more equitable basis. It would greatly reduce subsidies and the dangers of an export credit war.

#### **An interim measure**

Last week, the Participants in the Arrangement, some 22 industrial nations, met in Paris to consider the Wallen proposals. At the meeting, the European Economic Community announced that it was not yet ready to approve a differentiated rate system along the lines proposed in the Wallen Report. The Europeans did offer as an interim measure, however, to raise the present Arrangement minimum interest rates by  $\frac{1}{4}$  percent for poor countries and  $\frac{3}{4}$  percent for the intermediate and rich countries. This is a positive step in the right direction: It will reduce the subsidy by Participants on export credits this year by as much as several hundred million dollars.

By itself, the EEC offer was clearly inadequate. It is no substitute for real reform. But the EEC offer is without prejudice to consideration of a differentiated rate system. Moreover, at the Paris meeting, it was agreed that December 1, 1980, would be the deadline for reaching agreements on an acceptable revision of the Arrangement. This, then, is our major target: Agreement on basic improvements in the Arrangement by the end of this year.

#### **A more aggressive Eximbank—the second track**

At the same time we have sought through negotiations to reduce export credit subsidies, we have supported this effort by creating a more aggressive direct lending program at Eximbank. Our pace on this second track has been evident to both U.S. exporters and our foreign trading partners.

In FY 1977, Eximbank's direct loan program amounted to \$700 million. In FY 1978, Eximbank's direct loans were \$2.9 billion. We increased this to \$3.7 billion in FY 1979. In FY 1980, the administration went further still, and proposed a \$5.1 billion Eximbank, \$4.1 billion in direct budget funds and \$1 billion on a standby basis from the Federal Financing Bank (FFB). For FY 1981, the administration requested \$4.4 billion in direct loan funds and another \$1 billion FFB standby.

The Bank has made aggressive use of the substantial resources this administration has committed to it. In 1979, the Bank began to match, on a selective basis, the type of predatory financing addressed in Senator Stevenson's bill. Eximbank offered \$100 million to Tunisia at an interest rate of 5.5 percent to match the mixed credit offers of other countries. The Bank also matched foreign mixed credit competition twice in Cyprus and won. It has done this as well in Greece.

In addition to matching specific mixed credits, the Bank has matched foreign official credit competition generally. It has reduced its interest rates and increased its



participation in normal transactions. For example, the average Eximbank "cover" before the newly aggressive stance was approximately 40 percent. Now, it is over 55 percent. On nonaircraft cases, the cover is over 70 percent. The Bank's average interest rate on this increased cover has remained at about 8.3 percent.

The Bank's program of increased cover and relatively low interest rates has helped make U.S. exporters much more competitive when faced with officially supported finance from foreign sources. This, combined with other, more basic economic factors, has resulted in substantial growth in U.S. exports.

The volume of U.S. nonagricultural exports (excluding gold) did not grow at all from 1975 through 1977. But in 1978 such exports rose 8.2 percent by volume, and in 1979 the increase was 15.2 percent by volume and over 27 percent by value—more than twice the growth of world trade. Thus, the bottom line of our export expansion effort has been quite positive. Nevertheless, we must continue to press our trading partners (1) to agree to reduce subsidies on export credits and (2) to have a strong Export-Import Bank to match those trading partners who are recalcitrant in moving ahead on these negotiations.

### **Next steps in the negotiations**

The next 6 months will be the critical period of the negotiations. We must overcome the considerable objections that other countries have to adopting a differentiated rate system. No one should be under the illusion that all other countries are yet ready to accept a market-oriented approach to official export credit finance.

Some countries object to reducing the flow of subsidized export credits to developing nations because of North-South implications. Others use the North-South argument as a cynical excuse to subsidize exports. Other countries, without giving this excuse, use subsidized export credits to meet domestic adjustment problems. Still others believe that there is no practical relationship between interest rate differentials and exchange rate movements. Yet other nations wish to keep their rates low for reasons of monetary prudence.

Since these objections and our answers to them are the crux of the negotiations, I would like to explain them in some detail.

### **Export credits as aid**

A few countries are beginning to view official export credits as a means of transferring resources to the less developed countries, which are the principal borrowers. They argue that raising export credit interest rates would crimp the flow of resources to the LDC's. Subsidized resource transfers may seem especially necessary when most LDC's have been hit hard by oil import needs and are consequently experiencing balance of payments problems.

There are several responses to this line of argument. First, an export credit program should be viewed as a commercial program designed to facilitate exports through assumption, by the government, of various credit risks private creditors are unwilling to take. Export credit programs should not be seen as a substitute for genuine aid. If countries wish to increase the aid they give LDC's, they should do it through programs that directly benefit the LDC's rather than their own exporters.

Second, the main beneficiaries of official export credits are the richer LDC's such as Korea and Mexico, and the intermediate category countries such as the nations of Eastern Europe. These nations do not require aid nearly as much as countries that have low per capita incomes, if they need it at all.

Third, the sectors that benefit from official export credits are not necessarily the ones that most benefit the poorest segments of an LDC economy. The exports tend to be capital-intensive manufactured goods, while the truly poor people need help in more basic areas such as agriculture.

Finally, the World Bank, the regional development banks, the International Monetary Fund, and bilateral assistance agencies are far more efficient and effective in addressing development and balance of payments problems than are official export credit agencies. The purposes of the two sets of agencies should not be confused.

## Mercantilism

Another basis for export credit subsidies is, in essence, modern mercantilism. As we have reduced import barriers, some countries have invented less visible beggar-thy-neighbor policies.

These mercantilist countries have used official export credits as a tool to support troubled domestic industries and to promote their exports. Some national export credit programs are run on an entitlement basis, with virtually all exporters eligible for the subsidized credits. As a result, official export credit competition is one of the major trade issues remaining from the multilateral trade negotiations.

The rebuttal to the mercantilist argument is straightforward: Export credit subsidies work only if no other country is willing to match them. Over the last few years, it has become clear that export credit agencies are willing to match each other's programs. For example, our Eximbank had larger long-term direct credit programs in 1978 than Japan, the United Kingdom, France, or Germany.

In addition to this practical reason for avoiding export credit subsidies, there is another reason. The major trading countries agreed to restrict direct export subsidies in the multilateral trade negotiations. We hope that we can impress upon other countries the illogic of restricting subsidy practices in one area, but expanding them in another. Such practices run absolutely contrary to the efforts of industrial nations to facilitate the adjustment of their industries to changing world market conditions. While all governments assist selected industries from time to time, a program that entitles all industries to export subsidies contradicts both the basic concepts of positive adjustment and open trading relationships.

## Interest rate illusion

Another excuse sometimes offered for avoiding improvements in the Arrangement amounts to interest rate illusion. Buyers infected with this illusion are said to be concerned only with the nominal interest rate of a loan and not with the currency in which it is denominated. The supposed rationale for the illusion is that future exchange rates are unpredictable, and hence currency expectations are disregarded by foreign borrowers.

No one can predict with confidence what relative exchange rates will be in the future, but the existence of interest rate illusion is supported neither by experience nor by theory. Buyers ordinarily do have some exchange rate expectations in mind when considering competing export credit offers. Indeed, expected exchange rate movements are generally reflected in interest rate differentials. Nonetheless, those exporting nations that believe in the existence of interest rate illusion prefer the present Arrangement—with one rate for all currencies—to a differentiated rate system.

The practical answer to the proponents of interest rate illusion is that, under a differentiated rate system, all official export credit agencies would be able to offer export credits in any currency. If a buyer prefers low-interest credits in a foreign hard currency, then the official export credit agency could offer such credits.

## Future steps

As already noted, the next 6 months will be the critical period for the negotiations. The U.S. delegation to the OECD Ministerial on June 2-4 will make precisely the kind of points that I have outlined for you today.

Moreover, we expect similar discussions at the Venice summit. The President fully shares the view that an improved Arrangement is a priority issue for the summit. He is determined to press these negotiations to a successful conclusion. \* \* \*

We seek from both the OECD Ministerial and the Venice summit a clear directive that will support the reforms we have been urging over the past 3 years. To achieve this goal, we will need strong backing at both meetings from those countries who believe that increased export credit subsidization is a most undesirable practice.

We do not intend, however, to ignore the possibility that an improved Arrangement cannot be negotiated. If there is no progress in the next 6 months, we must consider the following steps in addition to those already taken during the past 3 years to make the Eximbank more competitive:

1. In specific cases, we might have to begin extending maturities should the budgetary cost of matching subsidized foreign interest rates prove too high. We could, for example, offer terms of 15 years for aircraft, or 20 or 30 years for powerplants.

2. Where countries have export subsidy programs which are particularly nettlesome to us, we would respond on a case-by-case basis in a manner designed to discomfort them to the maximum extent possible.

3. We would seek to enlarge the financial guarantee program, and make it more attractive to investors, so that it can relieve pressure on the direct loan budget. In this regard, we would seek to involve insurance companies, pension funds, and other long-term investors in export finance, an investment possibility they have not developed fully.

4. We would expand our efforts to establish common lines on financing individual transactions with countries in sympathy with our point of view. The International Arrangement has a "best endeavors" clause which promotes such efforts. In more than one instance we have been able to achieve informal agreement that reduced export credit subsidization is possible.

### **FFB standby**

In addition to these steps, Mr. Chairman, we would use the Federal Financing Bank standby proposed in the FY 1981 budget as a relief valve should we need to match foreign official credit competition more aggressively.

We are sympathetic to the concerns of the Congress about backdoor financing. But this is not backdoor financing. The Congress has full budgetary oversight in that the FY 1981 budget requests \$250 million in guarantee authority to cover the prospective \$1 billion FFB standby in FY 1980.

The administration has proposed limitations, for FY 1981 and beyond, on actual commitment levels for both direct loan and guarantee programs for all Federal agencies. Consequently, \$1 billion of the \$7.6 billion Eximbank limitation on guarantees and insurance authority sought for FY 1981 would be for the FFB standby arrangement.

The FFB standby has several advantages as a means of increasing Eximbank resources. First, it costs only 25 cents on the dollar against the FY 1980 budget authorization ceiling. In this respect, it has the same impact on the budget as does Eximbank-guaranteed money provided by the Private Export Funding Corporation.

Second, it does not entail budget outlays as the obligor would be a foreign borrower, even though the loan would be fully guaranteed by Eximbank.

Third, it would not burden the Federal budget with financing for projects that might not take place in a given year.

The FFB standby arrangement can act as a safety valve for Eximbank. Using it for projects whose financial needs and timing are relatively unpredictable will free an equivalent amount of direct credits for other exports. In this manner, it will be available for those transactions that would otherwise have disrupted the financial planning process.

Examples of such projects are powerplants, which are extraordinarily expensive and complex. The construction schedules of these plants are subject to unforeseeable postponements and delays. It is, as a consequence, exceptionally difficult to budget for them.

In a period of tight budget stringency, which we clearly face at present, the FFB standby appears to be a particularly attractive vehicle to promote our dual purposes of (1) assuring a fully competitive Eximbank and (2) thereby strengthening our negotiating position to improve the International Arrangement.

### **Pending legislation**

The administration appreciates that the two bills under consideration are also intended to improve the competitive position of U.S. exporters. The Competitive Export Financing Act of 1980 would authorize \$1 billion to allow Eximbank to provide export finance programs comparable to those offered by our principal competitors. The intent of the bill is to reduce and ultimately eliminate export credit subsidies.



The administration supports the intent of the bill. We may need it at some point in the future. But for now, we believe the \$1 billion of increased credit availability from the Federal Financing Bank on a standby basis is the preferable approach to providing Eximbank the necessary financial resources to match foreign official credit competition.

The second bill under consideration—S. 2340—would establish firm criteria for the Export Expansion Facility (EEF). We welcome this expression of congressional intent, but are fearful that expanded use of this facility may result in losses which may put further strain on the Bank's net income position during a period when it is already under pressure by matching foreign official credit competition. Moreover, earmarking further funds for the EEF will not, by itself, increase the total pool of resources available to the Eximbank. It is also our view that section 6 is unnecessary since Eximbank's retained earnings are sufficient to cover the risks attendant on the EEF and the Bank's other credit and contingent liabilities.

### Conclusion

The administration will continue to support a strong and fully competitive Eximbank. We will continue to seek improvements in the International Arrangement on Export Credits, to reduce and eventually eliminate the subsidy element in export credits, building on the modest but meaningful progress achieved over the past 4 years including last week.

This committee has strongly supported both efforts, for which we are deeply appreciative. We look forward to continuing to work closely with you as the process evolves toward achievement of the ultimate goals which I feel confident are shared among us.

\* \* \* \* \*

### **Exhibit 58.—Excerpt from remarks by Assistant Secretary Bergsten, July 9, 1980, before the National Foreign Trade Council, New York, N.Y., entitled "The Growing International Competitiveness of the U.S. Economy"**

It is always a pleasure to meet with the National Foreign Trade Council. On other occasions, I have addressed your group on the outlook for the U.S. balance of payments. As you remember, my forecasts have often been optimistic—and they have usually turned out to be fairly accurate. Today, I would like to address a related but even more fundamental issue: The international competitiveness of the U.S. economy.

Most observers seem to believe that U.S. international competitiveness is in secular decline. Press stories, speeches in international fora, and discussions with various U.S. exporters all imply a similar conclusion: that the United States has been losing trade competitiveness on a steady basis since the late 1950's. Support for this "conventional wisdom" often rests on the recent history of sizable trade and current account deficits.

My own reading of the situation leads to quite a different conclusion: that the U.S. international competitive position is quite strong today, and indeed ended the 1970's stronger than at the beginning of the decade. Let me turn to the facts that substantiate this view.

#### **U.S. trade in the 1970's**

The U.S. merchandise trade balance has of course deteriorated significantly over the past decade. In 1970, the merchandise trade account recorded a \$3 billion surplus. At the depth of the recession in 1975, the trade surplus rose to \$9 billion. Last year, while stronger than in 1978, the trade account was in deficit by about \$29 billion.

The source of this deterioration, however, is straightforward—and unrelated to the competitiveness of the United States in the world economy. The staggering increases in the cost of imported oil have not been offset by an equal increase in exports. Imported oil at the beginning of the decade cost the United States \$3 billion. Last year, the cost was \$60 billion and rising rapidly.

Had we maintained the 1970 balance on all other trade, the change in the oil bill alone would have produced an overall U.S. trade deficit of \$54 billion last year. Since our trade deficit was only about half that level—\$29 billion, to be precise—the balance on nonoil trade obviously improved. In 1970, nonoil trade was in surplus by \$5 billion. At the decade's end, this surplus had risen to \$31 billion. Even if we adjust for the impact of Treasury gold auctions, the surplus was about \$27 billion in 1979.

The primary reason for the improvement of \$20–\$25 billion was the growth in agricultural exports, which rose sharply from \$7 billion in 1970 to roughly \$35 billion last year. Many casual observers believe that the increased value of agricultural exports resulted primarily from higher prices. In fact, the volume of U.S. agricultural exports grew strongly—almost 7 percent per annum over the decade.

Those who believe we have been losing international competitiveness would argue that the United States has a natural monopoly on much of our agricultural exports and that for authentic competition we need to look instead at trade excluding agriculture. In fact, agricultural trade is highly competitive. But if the “conventional wisdom” that we have been losing competitiveness were correct, we should expect the nonagricultural, nonoil trade balance to have deteriorated substantially during the 1970's.

This has not been the case. Our balance on nonag, nonoil trade ended the decade with only a modestly larger deficit—\$5 billion—than the \$2 billion deficit in 1970. This balance did deteriorate substantially in the early 1970's, before the improved U.S. competitive position that developed during the decade was reflected in our export and import performance. In the last 2 years, however, this balance strengthened sharply. Let me elaborate.

### U.S. trade performance

The concept of international competitiveness is easy to describe, but difficult to measure statistically. I would define “international competitiveness” as the attractiveness, in both price and nonprice terms, of a country's export products and import substitutes compared with the goods produced in the rest of the world. No single quantitative measure is sufficient to determine a country's competitive position. Looking at an array of data, however, a general pattern for the U.S. competitive position emerges: The decade of the 1970's was a good one for U.S. international competitiveness.

The IMF publishes a series of data on international competitiveness, including 5 measures of price competitiveness for the 13 key industrial countries.<sup>1</sup> These series are adjusted for exchange rate changes to facilitate cross-country comparisons, and they are published in ratio form. The series measure the performance of a country against the weighted average of the other 12. Over the decade of the 1970's the U.S. position improved on all five measures. In particular:

- Relative U.S. export unit values improved by 12 percent;
- Relative U.S. wholesale prices improved by 21 percent; and
- Relative U.S. unit labor costs improved by 40 percent.

In other words, the United States became more competitive. These are little-recognized facts. Yet they portray important and impressive relative gains for the U.S. economy. On the basis of the same data, incidentally, Germany and Japan—the two countries usually held up as examples of superior performance—lost ground on all five measures.

These indicators suggest that the U.S. international competitive position is stronger than it was a decade ago. But improvements in competitiveness are not automatically, or even necessarily, translated into improved export performance. Competitiveness measures potential for increased exports or decreased imports. Whether or not exports in fact rise is a measure of the country's export performance.

In addition, there is a lag between changes in relative prices and resulting trade volume responses. Thus the usual performance measure for a given year reflects changes in international competitiveness in earlier years. Our own work suggests that it normally takes 2 or more years for a change in U.S. competitiveness to be fully realized in performance indicators such as trade flows.

<sup>1</sup> The series are relative unit labor costs, relative normalized unit labor costs, relative value-added deflators, relative wholesale prices, and relative export unit values.

The most commonly used measure of trade performance is export market shares. Most observers seem to believe that the U.S. export market share declined steadily during the 1970's and that this continued a trend begun in the late 1950's. The facts do not back up such a view.

In nominal value terms, the U.S. share of industrial country exports did in fact end the decade smaller than in 1970.<sup>2</sup> To get an accurate view of market shares, however, it is necessary to look at market shares in real terms. As the exports of countries whose currencies appreciated against the dollar during the period are converted from their own currencies to dollars, the statistical conversion process itself boosts the dollar value of their exports. Since the standard series on market shares are constructed in dollar terms, this in turn increases their market shares and reduces the U.S. share—without their exporting a single extra Volkswagen or Toyota. In short, the commonly used statistical series can give a very misleading impression of changes in the international competitive position of individual countries.

To alleviate this problem, we have constructed a series of market share data in real terms. On the basis of such volume data, U.S. market shares rose over the decade of the 1970's. Our real export market share did decline during the early 1970's, reaching a trough of 19.2 percent in 1971. But the very strong export volume growth of 1978 and 1979 resulted in a market share at the end of the decade of 20.3 percent—a full percentage point higher than the 1972 trough. This is a quite different result from that derived from the nominal data used by most observers.

I might add that, on the basis of this real market share data, Germany lost a full percentage point over the decade (15.9 percent in 1979 versus 16.9 percent in 1970). By contrast, Germany gained market share in nominal terms. In real terms Japan still gained substantially, increasing her share from 8.2 percent to 9.8 percent.

For the decade as a whole, the volume of total U.S. exports rose strongly. The total increase was 81 percent, a per annum growth rate—for all products to all markets—of 6.8 percent. Both agricultural and other exports grew at the same annual growth rate of 6.8 percent. Over the decade, world trade volume increased about 72 percent for a per annum growth rate of roughly 6.2 percent, less than the growth of U.S. exports. The data again reveal a rise in the U.S. share of world exports.<sup>3</sup>

Much of this U.S. gain occurred during the last 2 years. During 1978–79 U.S. export volume grew 10 percent each year. World trade volumes rose at only 5 ½ and 6 ½ percent, respectively. Hence the United States has been increasing its market share sharply in the most recent period.

Another commonly used indicator of competitiveness is the balance on manufactures trade. The U.S. trade balance on manufactures ended the decade in a higher surplus than in 1970 (\$4.4 billion in 1979, \$3.4 billion in 1970). During the first 5 months of 1980, the surplus rose to an \$8.4 billion annual rate. Again, our basic position has strengthened.

### Service exports

Continuing growth in the surplus on services also helped strengthen the U.S. current account position during the seventies. The services sector has received little attention in most analyses of either the U.S. external position or our basic competitiveness, but it has become a large and growing part of U.S. international activity.

As recently as 1970, gross flows in the services sector were only about \$43 billion. By 1977, total U.S. trade in services had grown to \$105 billion. When I spoke before this council in November 1978, I suggested that services flows could total \$140 billion in 1979. In fact, I grossly underestimated the strength of the service sector; during 1979, gross service flows totaled \$175 billion. This fourfold increase in the decade kept pace with the fast growth in the value of U.S. merchandise trade.

<sup>2</sup> It should be noted that developing countries seized a growing share of world exports of manufactured goods during the 1970's, reducing the share of industrial countries as a group and of most individual industrial countries. Unfortunately, there exist no consistent data series which permit a systematic evaluation of their importance. Lags in data detail and absence of consistent price deflators also delay timely analysis; we therefore use throughout the standard series of export data for the 19 major OECD countries.

<sup>3</sup> This is a different, broader calculation than used in the preceding paragraphs, which was linked to shares of developed country exports only.



From 1970 to 1978 the U.S. surplus on services grew from \$3 billion to \$25 billion. In 1979 it jumped sharply to almost \$35 billion. The "invisibles" surplus, after deducting private remittances and Government grants of \$5 ½ billion, was about \$29 billion—almost wholly offsetting the merchandise trade deficit and producing near balance in our current account.

Net direct investment income accounted for almost all of the improvement over the decade. During the seventies, the surplus on direct investment income increased from a little more than \$7 billion to nearly \$32 billion. The level of this item was affected by a change in statistical treatment which we instituted in 1978 to conform the U.S. presentation to that of all other countries as recommended by the IMF guidelines. As a result of that change we now count reinvested earnings as an income receipt—and their reinvestment as a capital outflow. But the strong growth in this sector is unaltered by the definitional change: The surplus on remitted earnings alone rose from \$4 ½ billion to \$17 ½ billion over the decade.

## Outlook

Where is the balance going from here? Between the first quarter of 1978 and the first quarter of 1980, the nonoil, nonag trade balance improved from a deficit of \$7.8 billion to a small surplus of \$0.3 billion. This \$32 billion gain (annual rate) is impressive.

It is doubtful that our position will continue to strengthen at this pace. Nevertheless, the direction of further change seems clear at least in the short run. The U.S. recession will clearly strengthen our current account position. From March through May, as the recession hit, our current account returned to rough balance as exports continued to grow and imports (including oil imports) dropped sharply.

Perhaps as important, from a longer term perspective, has been the slowing of oil imports. Higher prices to consumers are obviously reducing demand. During the first 5 months of this year, oil imports were running 12 percent below the same period last year. At today's prices, this represents a saving of over \$10 billion on imported oil. I believe that we will continue to see declines in the volume of oil imports.

Aside from price competitiveness, which I have already addressed, the other basic determination of trade flows is income growth. The U.S. trade balance is affected strongly by relative growth rates at home and abroad. Improvements in the U.S. trade balance or current account would provide little cause for optimism if they derived solely, or even importantly, from a slowdown in our own economy. In an effort to gain a better understanding of the underlying trade and current balances, we have therefore attempted to look at cyclically adjusted positions as well.

This is a very tricky area, and the results can be taken only as rough orders of magnitude. But the range of available estimates suggests that the United States was operating closer to full employment in 1979 than were our major trading partners. Had all major trading countries been operating at something like full capacity, the underlying U.S. trade balance would therefore have been considerably stronger. Our imports might have been \$7–\$10 billion higher, but our nonagricultural exports would have been \$15–\$20 billion larger. Thus our cyclically adjusted trade deficit last year might have been around \$20 billion rather than the \$29 billion deficit actually recorded. Our current account would have been in sizable surplus.

Hence cyclical factors do not obviate the encouraging recent trends in the U.S. external position. It is impossible to put forth precise numbers, but it seems that the U.S. current account will be at least in rough balance for the 3-year period 1979–81, which is about as far ahead as anyone can hope to see. Last year was virtually in balance. We had a sizable deficit in the first quarter of this year as the big OPEC price increase passed into the import statistics, but the last few months saw a return to rough balance. Our latest estimates suggest an even stronger picture into 1981. The 3-year picture appears to be, at a minimum, one of rough equilibrium.

## Conclusion

I have presented a relatively optimistic view of both U.S. international competitiveness and the outlook for our current account. From a policy standpoint, however, we clearly cannot rest on past achievements. Exports are an essential and growing element of the U.S. economy, generating substantial employment and production at

home. Export expansion provides the only appropriate means of paying for the increased cost of needed imports, including oil. With economic growth slowing throughout the world, the competition for export markets will be fierce.

Hence the United States must compete even more effectively in world markets in the future. Strong efforts will be needed by both U.S. industry and the U.S. Government to take full advantage of the strong underlying competitive position which I have described today—and to improve it further in the future.

We can do so, however, on the basis of a U.S. export performance over the past decade that has been considerably stronger than most observers recognize. The fundamental competitive position of the United States has improved. There is no reason to believe that U.S. exports are less attractive than those of other countries. Given the appropriate stimulus and support, our export performance can be improved further, thereby helping to meet a number of cardinal economic objectives of the United States for the foreseeable future.

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**Exhibit 59.—Excerpts from statement by Assistant Secretary Bergsten, September 9, 1980, before the Subcommittee on Consumer Protection and Finance of the House Committee on Interstate and Foreign Commerce, regarding the administration's views on H.R. 7791, the Reciprocity in Foreign Investment Act**

I appreciate the opportunity to appear before the subcommittee today to present the administration's views on H.R. 7791, as Chairman of the interagency Committee on Foreign Investment in the United States (CFIUS)—which is responsible under Executive Order 11858 for monitoring the impact of foreign direct investment in the United States and for coordinating implementation of U.S. policy on such investment. This bill, the Reciprocity in Foreign Investment Act, has the potential to affect foreign direct investment in the United States significantly. \* \* \*

**U.S. policy**

It is the fundamental policy of the U.S. Government to welcome foreign investment to this country and extend national treatment to foreign-owned firms based in the United States. However, we do not actively promote—nor of course do we discourage—inward or outward international investment. We believe that foreign investment, like all investment, makes a maximum contribution to society when it responds to market forces. We therefore believe that the Government should normally avoid measures which give special incentives or disincentives to investment flows, or to the activities of individual companies regarding international investment.

\* \* \* \* \*

**Benefits of U.S. policy**

This policy has served our Nation well. Increased investment is an objective of all nations, including the United States. It means more jobs, more productive capacity, and more technology. It means more exports and more capital inflows to strengthen the balance of payments and the dollar. It means more competition to help combat inflation.

\* \* \* \* \*

**Fear of foreign control**

Since the early 1970's, concerns have occasionally been expressed that there is too much foreign investment in the United States, and that foreign countries through their investments here may take control of the U.S. economy—or at least important sectors of it. Those fears are plainly absurd. Despite the substantial amounts of foreign investment in the United States, foreign interests control an extremely small share of the U.S. capital stock.

The Commerce Department has estimated that, in 1977, U.S. affiliates of foreign corporations accounted for only 2 percent of the employment of all U.S. businesses except banks. They accounted for less than one-half of 1 percent of privately owned U.S. land. They accounted for 2.6 percent of the total value added for the U.S. economy as a whole.

These percentages have clearly risen a bit in the last 2 years, but they are still tiny. The numbers are tinier yet for the OPEC countries, which are sometimes singled out for particular concern; they own something like one one-hundredth of 1 percent of the capital stock of U.S. companies.

It is also curious to observe U.S. fears regarding foreign influence over our national economic interest in light of the vastly higher proportion of businesses in other countries owned by foreign—predominantly U.S.—firms. In Canada, for example, over 55 percent of manufacturing industry is owned by foreigners, as is 31 percent of its nonfinancial industry. U.S. firms alone control 43 percent of Canadian manufacturing. The number is somewhat lower in Europe and in big developing countries such as Mexico or Brazil, but they are far higher than the tiny ratios of foreign ownership here in the United States.

Despite the relatively huge ownership interests of U.S. firms in various foreign countries, these countries—with the occasional exception of Canada—do not exhibit the kinds of fears which are now occasionally voiced in the United States. There was concern in Europe a decade ago over “Le Defi Americain”; that concern has now virtually disappeared. Nearly all countries have learned that ownership does not imply control, nor does control require ownership. In most foreign countries, concern over foreign ownership has diminished to a point where it is no longer a major issue.

### Global trends

For that same reason, however, there are some important and disturbing global trends with respect to national policies toward foreign investment. Governments at both the federal and subfederal levels are seeking to both attract and control the impact of such investment (rather than worry about who owns it). In so doing they are adopting measures which can distort the allocation of investment among nations, reduce the gains from international specialization, reallocate the benefits of investment from one country to another, and prompt countermeasures by other governments.

Major problems arise from two related directions. One is the use by governments of financial, trade, tax, and other incentives to attract foreign investment which might otherwise locate elsewhere, and thus rearrange the location of production. The second is their imposition of performance requirements which seek to tilt the economic benefits stemming from particular investments to one country at the expense of others.

A critical question for U.S. policy, now and in the future, is whether to emulate this trend ourselves or to continue to oppose it; i.e., should we fight them or join them? It seems clear to this administration that we should fight them, and not reverse our policy by erecting barriers to the free flow of investment and other activities.

The economic and political price of such a reversal would be high. As I have already noted, we have an open door for foreign investment in this country because such investment provides new productive capacity, new technologies, and more exports to create jobs, strengthen the dollar, help improve our balance of payments, and fight inflation. These needs are particularly apparent now. A policy reversal would, in all likelihood, discourage foreign investments in the United States and be particularly damaging to the U.S. economic well-being.

In addition, a reversal in U.S. policy would redound to the disadvantage of U.S. investment abroad. These investments now total over \$190 billion. Income from them strengthened our current account by \$37.8 billion last year, fully offsetting our deficit on merchandise trade and thus sustaining the dollar. It would be sheer folly to invite negative foreign actions toward this huge stock of U.S.-owned investment.

At the international level, a reversal of U.S. policy would almost certainly kill our efforts to develop new agreements governing the use of incentives and performance requirements which, as noted already, are important problems with potentially adverse effects on the U.S. economy. The United States is the leader in pressing for agreement in these areas; if we changed course, the effort would collapse. We fully



recognize that progress in this fight against government measures which distort international investment will take time, but we believe that progress is being made.

\* \* \* I would like to give the subcommittee a brief report on the activities of a Task Force on Private Foreign Investment of the Development Committee of the IMF and World Bank which I have had the pleasure of chairing. The Committee established the task force in late 1978 to examine home and host government policies that affect the direct investment process and development. The task force, composed of developed and developing country representatives, will be presenting its final report to the next meeting of the Development Committee here in Washington—in conjunction with the annual meetings of the IMF and World Bank—in late September. Despite the diverse interests and policies of the countries represented, the task force inter alia—

- Recognized that performance requirements, while they are designed to enable host countries to ensure that they obtain adequate benefits from incoming investments, may in some cases work to their disadvantage and may also, under certain circumstances, discourage investment or produce distortions in the economy of the host country;
- Noted that, in view of the widespread use of incentives by host countries, countries offering them may not do much to improve their competitive position but rather may simply increase the profits of the firms and the taxes paid to the investors' home country treasuries;
- Agreed that the use of performance requirements and incentives by one country may have adverse effects on others, for instance, by diverting investment from other countries to their own, thus provoking retaliation and/or emulation by the "losing" countries;
- Noted in this connection that performance requirements could become tantamount to a restrictive trade practice and more generally cause distortions in trade flows;
- Endorsed the objectives of seeking an international understanding which would limit the adverse effects of incentives and of considering what further actions might need to be taken concerning performance requirements, and decided in some detail what an arrangement to limit incentives could look like; and
- Recommended that the World Bank group study and analyze existing foreign investment incentives and performance requirements and, depending on the outcome of the study, consider making an attempt to develop a concept and terms upon which an understanding to limit the adverse effects of such measures might evolve.

This is a modest, but significant, step toward dealing with today's real problems concerning international investment. \* \* \* Having led this effort so far, the United States should not jeopardize it by acting unilaterally to deter incoming foreign investment.

## H.R. 7791

With all this as preamble, let me now focus on H.R. 7791. The proposal takes a more moderate approach to monitoring and controlling foreign direct investment in the United States than other proposals that have been put forward. Nonetheless, it raises many problems:

- It would be taken around the world as a signal that the United States had shifted its historic position and become less open to incoming foreign investment. It would therefore clearly discourage such investment, denying us the kind of benefits outlined earlier at a time when these benefits—jobs, capital, technology, exports—are sorely needed.
- It would produce an impossible administrative task: Investors from several countries with diverse investment policies wishing to invest in the same U.S. industry or company would be subject to completely different rules, based on each foreign government's policies with respect to their incoming foreign investment.

- Such action would clearly undermine the progress we have made thus far in attacking the major problems of incentives and performance requirements, and would almost certainly jeopardize any future attempts to arrive at a multilateral agreement in this area.
- Other countries would react negatively to such legislation, making conditions worse for U.S. investment abroad and, perhaps, even jeopardizing the massive flow of direct investment income which is a great source of strength for the dollar and our balance of payments. For these reasons, the administration opposes H.R. 7791.

**Exhibit 60.—Opening remarks by Secretary Miller, September 16, 1980, at the first meeting of the U.S.-China Joint Economic Committee, Washington, D.C.**

Premier Bo, it is a particular pleasure to open the first formal meeting of the U.S.-China Joint Economic Committee. On behalf of my colleagues here who represent many different departments and agencies of the U.S. Government, I extend a warm welcome to you and your delegation.

We are pleased that the process of economic normalization has moved forward so rapidly. This process was initiated when Vice Premier Deng Xiaoping and President Carter met in January 1979 and established this Committee. My predecessor, Treasury Secretary Blumenthal, went to China 1 month later to discuss the structure of the Joint Committee and to begin a dialog on numerous bilateral economic issues. Since then there have been many visits of our economic officials. Trade has grown sharply, reaching \$2.3 billion in 1979, almost double that of 1978, and approaching \$4 billion this year. Important agreements have been signed and implemented as we have moved step by step to build a framework for the orderly growth of economic ties. These include a claims settlement agreement which, among other things, facilitated the expansion of U.S. correspondent bank relations with the Bank of China from a mere handful 20 months ago to approximately 50 presently; a trade agreement which extended most-favored-nation treatment; an agreement on trade exhibitions that led to your exhibition that opened in San Francisco a few days ago; and scientific and technology agreements in more than 16 fields. This includes a protocol on hydropower cooperation which is potentially among the most important in terms of China's development and U.S. commercial opportunities.

Most dramatic has been the sharp increase in the flow of visitors and delegations between our two countries. An average of 100 Chinese delegations visit the United States each month and more than 60,000 Americans are expected to visit China this year. The visit of the delegation of the Machine Building Industry Commission, one part of Vice Premier Bo's trip to the United States, is an example of the many important Chinese groups now visiting our country.

This meeting of the U.S.-China Joint Economic Committee provides an opportunity to bring to a final conclusion a number of important agreements that have been under negotiation. These include agreements in the fields of civil aviation, maritime, consular offices, and textile trade.

This meeting will provide an equally important opportunity to review the progress we have made in economic normalization and the steps we need to take in the future. Our agenda includes such topics as facilitation and promotion of business and trade, and finance and investment issues including Overseas Private Investment Corporation guarantees for U.S. investment in China and Export-Import Bank lending. We will also exchange views on the economic situation in our two countries.

In sum, we are prepared to consider the broad scope of economic, trade, finance, and investment issues that are of concern to our two countries and essential to the expansion of our overall relationship.

## Commodities and Natural Resources

### Exhibit 61.—Statement of Assistant Secretary Bergsten, March 4, 1980, before the Subcommittee on Treasury, Post Office and General Government of the House Committee on Appropriations, entitled "Appropriation of the U.S. Contribution to the International Natural Rubber Agreement"

I am pleased to appear before you today to testify in favor of an administration request for an \$88 million appropriation for the new International Rubber Agreement. This appropriation is necessary to support U.S. membership in the International Rubber Agreement for which the administration will be seeking the advice and consent of the Senate as well as authorizing legislation.

The Treasury Department strongly supports ratification of this agreement and recommends approval of the appropriation at an early date to serve as an important element in the administration's anti-inflation program. In calling attention to the need to fight inflation, President Carter has made prominent reference to international commodity trade and the potential role of international commodity agreements in contributing to the battle against inflation in the United States:

- When prices of raw materials and food fluctuate upward, the effects tend to spread throughout the economy, raising prices and wages generally \* \* \*. Reducing fluctuations in commodity prices, therefore, helps to reduce inflation.

This objective was reaffirmed in the administration's testimony before the Senate Budget Committee recently when Secretary Miller and others stated that "properly constructed commodity agreements can provide benefits to both producers and consumers by reducing inflationary pressures, promoting greater stability, and increasing incentives for primary commodity production." They went on to point out that the rubber agreement provides an excellent example of an international commodity arrangement which balances producer and consumer interests to their mutual benefit.

Approval of this appropriation will demonstrate the firm commitment of the U.S. Government to the agreement and to our overall international commodity policy. It is important to note that, while this agreement will contribute to rubber price stability, it will not provide any artificial prop for rubber prices.

My colleague from the State Department will describe the planned operation of the agreement and details of this U.S. contribution. I would like to focus my remarks on overall U.S. commodity policy and how the Natural Rubber Agreement is a major element of that policy.

#### Administration commodity policy

One of the early international economic policy decisions made by this administration was to reorient U.S. policy from leaving commodity trade to the vicissitudes which are characteristic of commodity markets to seeking deliberate measures to reduce instability in prices and supplies. This reorientation reflects the administration's continuing concern about the adverse effects of volatile commodity prices on inflation in the United States, on the economies of all exporting and importing countries, on individual producers and consumers, and on the orderly expansion of raw material supplies.

Prices of primary commodities are exceptionally unstable and the U.S. economy experiences real costs from such price instability. For example, excessive rises in commodity prices, even when they are temporary, induce economywide price increases beyond the direct impact of the commodity prices themselves. This is because producers of manufactured goods and food processors often justify additional increases in their prices on the basis of cost increases stemming from rising prices for their raw materials. However, these increases are not likely to be withdrawn when raw material prices subsequently recede. The effect is a ratcheting up of the general Consumer Price Index, which in turn provides justification for higher wage increases. As inflation spreads, for this as well as other reasons, inflationary expectations then generate additional demand for business inventories and create fears of impending



shortages, provoking protective purchases and forcing raw material prices up even further in a spiral which, as we saw particularly in 1973-74, can be devastating.

Excessive price declines for commodities can also, paradoxically, fuel inflation over the long run. When such declines are precipitate and extended in time, they can deter investment in new productive capacity at both the primary and processing stages. Supply then becomes inadequate to meet the normal growth of demand in future years, pushing prices up at that time.

These two occurrences are peculiar to some, though not all, of the commodity markets because prices in these markets fluctuate much more sharply than do prices either of industrial products or of services.

It is often argued that the market provides the optimal degree of price stability for commodity trade. Unfortunately, this is not always the case. The direct benefits of reducing commodity price fluctuations accrue to all buyers and sellers, whether or not they individually contribute to the cost of the stabilization arrangement; hence the incentive to individual market participants to contribute to the cost of stabilization is negligible, and the market alone will not call forth the appropriate institutions. In addition, the indirect benefits of price stabilization—notably the reduction of overall inflation rates—extend well beyond the universe of participants in the commodity markets themselves. Thus, price stability can be considered a public good, and an appropriate target for governmental action.

Economies of exporting countries also suffer significantly as a result of gyrating commodity prices. Many of these exporters rely heavily on commodities for their foreign exchange earnings, which are used largely to buy industrial products needed for development. The United States is among those who supply substantial amounts of exports to commodity-exporting countries. In 1979, we sold \$5.2 billion to natural-rubber-producing countries, a more than 30-percent increase over 1978. Extreme volatility in commodity prices weakens the ability of the United States to maximize our export potential to these countries.

It was against this background that the administration decided to launch a series of steps to help contain inflationary pressures emerging from commodity markets, reduce our vulnerability to unreliable and uneconomic sources of supply, and enhance economic stability in producing countries. This U.S. policy embodies the following elements:

- Negotiation of international commodity agreements, where feasible, between producers and consumers to reduce excessive price volatility;
- Emphasis on buffer stocking as the preferred price-stabilizing mechanism;
- Joint financial responsibility for financing such agreements;
- Promotion of increased investment in commodity industries;
- Negotiation of a common fund to facilitate financing of individual agreements; and
- More effective operation of the Compensatory Finance Facility of the International Monetary Fund to buffer the effects of fluctuations in a country's export earnings.

The United States now belongs to the coffee, sugar, and tin agreements, which all contain market intervention mechanisms which rely to some extent on commodity stocking to achieve their objectives. The United States joined the coffee agreement in the 1960's and became a member of the tin agreement in 1976 after participating in its negotiation a year earlier. Negotiation of the sugar agreement, with the United States playing a major role, took place in 1977, and the Senate ratified the agreement late last year. The Congress early this year authorized a U.S. contribution to the tin agreement to stabilize prices.

### **Structure of the rubber agreement**

Countries involved in exporting and importing rubber have recognized for some time the desirability of a commodity agreement for rubber to alleviate volatile market conditions.

The volatility of rubber prices is well documented. For example, a recent World Bank study of the volatility of the prices of 40 commodities showed that rubber ranked

seventh. The attached graph shows the wide fluctuations in natural rubber prices during the past 20 years. The New York price declined in an irregular fashion from 38 cents per pound in 1960 to 20 cents in 1968. It then rose to 26 cents the next year before resuming its downward trend to 18 cents in 1972. This low was followed by a new peak of 39 cents in 1974. After another sharp break to 30 cents in 1975, the price has soared, reaching nearly 80 cents a pound in mid-February. It has now dropped back to about 70 cents.

Because of their concerns about these price fluctuations, producing countries reached agreement among themselves to establish a small buffer stock and institute export controls to seek to stabilize rubber prices. It was only after importing countries demonstrated a sincere effort to negotiate a producer-consumer agreement that the producers agreed to hold their agreement in abeyance.

All countries agree that a producer-consumer arrangement would be more effective in stabilizing the natural rubber market and provide a better balance of benefits to producers and consumers. Accordingly, the producing countries have agreed to abandon their proposed agreement when the new natural rubber agreement goes into force.

We believe price stabilization agreements should operate wherever possible through buffer stocks. The structure of the rubber market is well-suited to a buffer stock arrangement. Bought when prices are low, and sold when they are high within an agreed price range, buffer stocks can be more effective than any other approach in stabilizing prices without distorting markets or production patterns. In fact, we expect them to make profits to help cover operating costs.

Buffer stocks are far preferable to supply controls regarding market efficiency, operational simplicity, and consumer benefits as they allow the price mechanism to allocate resources to the most efficient producers. There are three basic criteria which must be met for this, our preferred approach, to apply to a given commodity. First, the international price must be established in an open market. Second, the commodity should be either nonperishable or easily rotated in storage facilities so that stock maintenance is feasible and carrying costs do not become exorbitant. Third, the commodity should be relatively homogeneous in the sense that most trading takes place in a limited number of well-defined grades whose prices move in tandem. In addition, a buffer stock must have large stocking authority, adequate financing shared by both producers and consumers, an adjustable price range, and membership by all major producers and consumers.

There is wide agreement that the natural rubber market meets these criteria. I particularly want to emphasize that this agreement will provide for: A large buffer stock of 550,000 tons; a wide price band of plus or minus 20 percent around a reference price; and provision for adjustment of this range as market conditions change. In fact, this agreement will come close to being a prototype commodity agreement.

Furthermore, the agreement contains provisions under which producing countries will implement policies to ensure availability of rubber supplies and will not undertake actions which are inconsistent with the agreement. In addition, the Council may make specific recommendations to governments on policies affecting supply and demand for rubber.

In achieving this high degree of success in negotiating an effective agreement, we need to recognize the spirit of cooperation among the participants in the conference. The major rubber producers from Southeast Asia in particular worked long and hard to assure a successful outcome. Those countries fully appreciate that stabilization will promote a more efficient industry.

### **Appropriation of the contribution**

As a member of the natural rubber agreement, the United States will be obligated to finance its share of the costs of acquiring and operating the buffer stock. The costs of the agreement are to be shared equally between producers and consumers. We have estimated the U.S. share will be \$88 million, or about 12.5 to 15.5 percent of the total requirement. This approximates our share of trade in natural rubber. We expect that the appropriation will be on a one-time basis, and the amount of money to be paid in FY 1981 will be relatively small—perhaps \$5 million.

This small initial payment will enable the agreement to set up its administrative machinery and begin purchasing a buffer stock quickly, if necessary. The remainder of members' contributions would be made as needed to the buffer stock manager to enable him to expand his purchases to keep prices within the price range.

We recognize that budgets must be kept tight in this difficult period, but the administration has carefully considered the need for this appropriation and feels it is imperative that it be appropriated this year.

By doing so, the natural rubber agreement, an important element in the administration's international commodity policy, will contribute to our long-term fight against inflation. It will also provide benefits for the producing countries. But in order to set these mutual benefits in train, we and others must do our part by providing funding to permit the agreement to become operational. By doing so, we are following a course similar to that established by our contribution to the tin agreement.

### **Policy implementation**

We have made substantial progress in implementing U.S. commodity policy, though the task has been long and arduous and much work remains. The successful negotiation of the rubber agreement is but the latest achievement in the commodity area. Other accomplishments are:

- Successful negotiation and ratification of the International Sugar Agreement with its special stocking provisions;
- Congressional authorization to contribute tin to the international tin buffer stock in proportion to our imports;
- A commitment by all countries to share financing of commodity agreements;
- Significant progress in negotiating a common fund;
- Action by some commodity-producing countries to reexamine and, in some cases, modify their tax policies to reduce deterrents to investment in commodities;
- Adoption by the multilateral development banks and our Overseas Private Investment Corporation of policies to allocate more loans to raw materials industries in developing countries; and
- Liberalization of the Compensatory Finance Facility of the IMF which has resulted in gross drawings of \$4.8 billion since 1975, compared with \$1.2 billion in the 13 years of its prior operations.

There have been disappointments along the way in achieving these goals, but we have established precedents which should lead to future achievements.

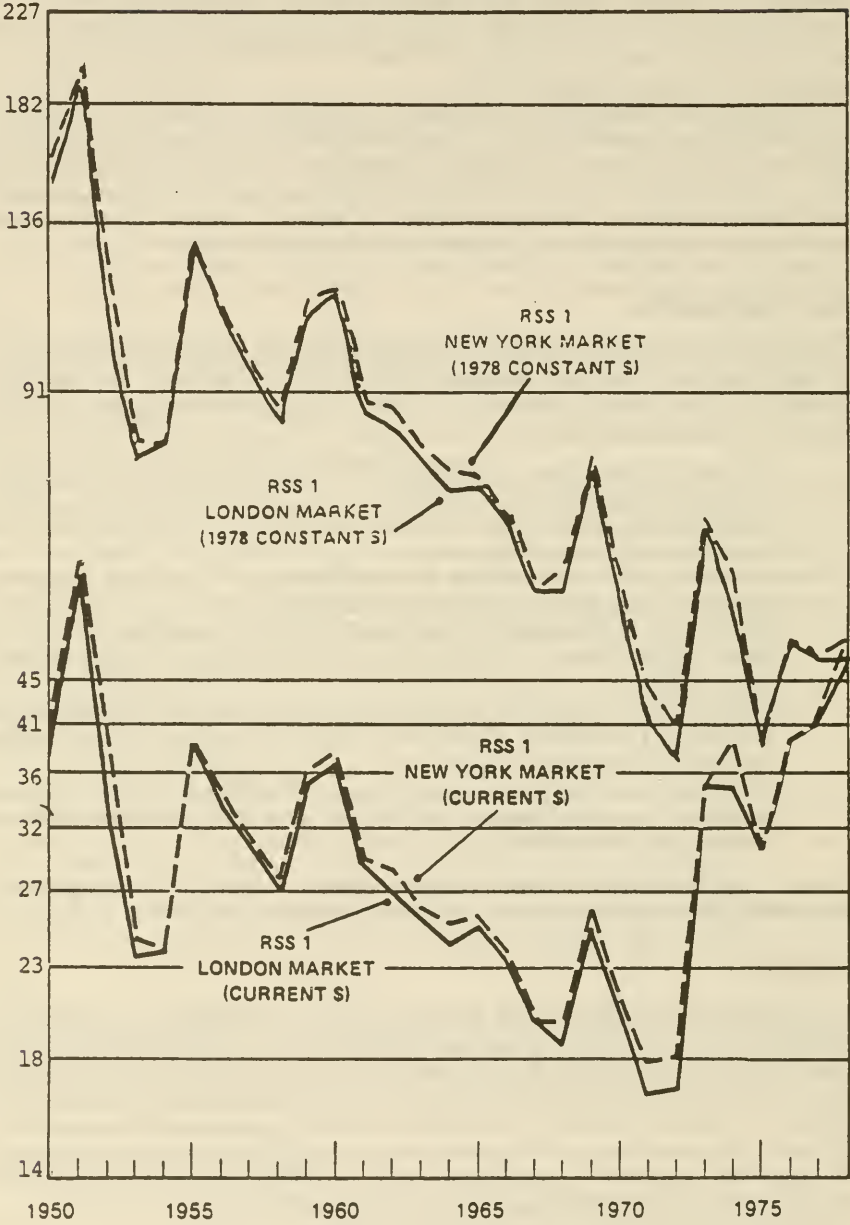
### **Conclusion**

In conclusion, I would like to reemphasize that the administration is strongly committed to an international commodity policy which will help fight inflation in the United States and worldwide. We have made substantial progress in implementing it. This natural rubber agreement will become a strong component of that policy, and represents a serious cooperative effort between importing and exporting countries. It will lead to the abandonment of the producer proposal for a natural rubber agreement. We expect the agreement to significantly moderate rubber price fluctuations over the long run and be well worth the modest cost to the United States.



**NATURAL RUBBER**  
**(YEARLY AVERAGE)**

US CENTS/LB



SOURCE: Department of Treasury  
World Bank Data

## International Monetary Affairs

### Exhibit 62.—Communique of the Interim Committee of the Board of Governors of the International Monetary Fund on the International Monetary System, October 1, 1979, issued after its 13th meeting in Belgrade, Yugoslavia

I. The Interim Committee of the Board of Governors of the International Monetary Fund held its thirteenth meeting in Belgrade, Yugoslavia, on October 1, 1979 under the chairmanship of Mr. Filippo Maria Pandolfi, Minister of the Treasury of Italy, who was selected by the Committee to succeed Mr. Denis Healey, formerly Chancellor of the Exchequer of the United Kingdom. Mr. Jacques de Larosiere, Managing Director of the International Monetary Fund, participated in the meeting. The following observers attended during the Committee's discussions: Mr. Gamani Corea, Secretary-General, UNCTAD; Mr. Rene Larre, General Manager, BIS; Mr. Emile van Lennep, Secretary-General, OECD; Mr. Fritz Leutwiler, President, Swiss National Bank; Mr. Olivier Long, Director General, GATT; Mr. Robert S. McNamara, President, IBRD; Mr. Rene G. Ortiz, Secretary General, OPEC; Mr. Tommaso Padoa-Schioppa, Director General for Economic and Financial Affairs, CEC; Mr. Jean Ripert, Under-Secretary-General for International Economic and Social Affairs, UN; Mr. Cesar E. A. Virata, Chairman, Development Committee.

II. The Committee discussed the world economic outlook and the policies appropriate in the current situation.

The Committee noted that events in recent months pointed to a period of reduced economic growth in the industrial countries. Signs of a recession in the United States had become stronger, and some slowing of economic expansion in other industrial countries was in prospect. However, the continuation of a positive growth rate in these other countries should serve to limit the degree of the expected international slowdown.

The Committee observed with great concern that inflation throughout the industrial world had intensified. In view of this grave threat to economic and financial stability, the Committee emphasized that the main task of economic policy was to contain inflationary pressures and to reduce inflationary expectations. One of the immediate problems was to prevent the recent surge of price increases for oil and other primary products from adding to the strength of inflationary expectations and thus being built into underlying rates of increase in wages and prices. Accordingly, the Committee noted with satisfaction that reduction of inflation was being given priority in the economic policies of industrial countries, and it reiterated its view that in many countries progress in reducing inflation was an essential precondition for the resumption of vigorous economic growth.

On the external side, the Committee noted the very large shifts in current account balances that were occurring both among and within groups of countries. With the current account surplus of the major oil exporting countries expected to rise sharply, a corresponding deterioration in the combined current account balance of the oil importing countries as a group was obviously in prospect.

Although the industrial countries were expected to account for most of this deterioration in 1979, the problem of the distribution of current account surpluses and deficits among the major industrial countries—a matter of concern over the past few years—now appeared to be receding. This improvement in the pattern of payments imbalances was attributable in large part to offsetting changes in demand conditions in the largest countries and to effects of past exchange rate changes, and was seen by the Committee as important evidence of a better working of the international adjustment process. In this connection, the Committee welcomed the closer cooperation in intervention policies in the exchange markets.

Noting that the combined current account deficit of the non-oil developing countries was expected to increase from about \$32 billion in 1978 to \$45 billion in 1979 and to well over \$50 billion in 1980, the Committee expressed concern that this development would lead to an increase in external financial difficulties among these countries. Particularly disturbing was the prospect of a further rise in debt service charges, which in a number of developing countries were already rising faster than the rate of increase in the debt itself.

The Committee also noted with concern the fact that the worsening of the external position of the non-oil developing countries was occurring at a time of growing internal strains. While economic growth in the developing world was in general being fairly well maintained, it remained modest in relation to population growth and developmental needs. Moreover, the problem of inflation, already quite serious in many developing countries, had intensified in 1979.

The situation of the non-oil developing countries, the Committee observed, called in many cases for an improvement in domestic financial policies. It also underlined the need for a larger flow of external resources. It was especially important, in the Committee's view, that the industrial countries, in the design of their economic policies, pay particular attention to the economic needs of developing countries. In this connection, a wide range of policies was seen to be relevant, including the reduction of protectionist measures; the opening of import markets to exports of manufactures and commodities from developing countries and of capital markets to outflows of funds to such countries; and measures to give new impetus to the flow of official development assistance, which had stagnated in recent years.

III. The Committee reiterated its view on the necessity of an active exercise by the Fund of its surveillance authority as a means of strengthening the adjustment process.

IV. The Committee noted with satisfaction that since its last meeting there had been a number of developments that enhanced the Fund's ability to provide balance of payments assistance to its members. It welcomed the adoption by the Executive Board of a new set of guidelines on the conditionality applicable to the use of the Fund's general resources in the upper credit tranches and the improvements in the Fund's compensatory financing facility, including the increase in the maximum amount of compensation that could be obtained under that facility.

The Committee also noted with satisfaction that, since the supplementary financing facility became operational in February, the Fund has begun to use the additional financial resources which have been put at its disposal to provide members experiencing difficult adjustment problems with assistance in larger amounts and for a longer period than could be made available under the regular credit tranches. In this connection, the Committee, like the Development Committee, asked the Executive Board to give attention to developing ways and means of lowering the interest costs of the supplementary financing facility.

The Committee also agreed with the request of the Development Committee to the Executive Board to give further consideration to increasing the maximum repurchase period in respect of purchases under the extended Fund facility from eight to ten years.

The Committee agreed to keep the adequacy of these measures under review.

V. The Committee recognized that there was a clear need for broad multilateral efforts to assist member countries in coping with the very difficult situation ahead. In this context the Program of Immediate Action outlined by the Group of 24 and endorsed by the Group of 77 would be kept in view.

VI. The Committee noted the slow progress in the implementation of the increases in quotas approved under the Resolution of the Fund's Board of Governors on the Seventh General Review of Quotas. In view of the importance of an early implementation of these increases in quotas, the Committee urged those members, especially those with the larger quotas, that have not yet taken action that would enable them to consent to the increases in their quotas, to do so as promptly as possible.

VII. The Committee considered the report submitted by the Executive Board on the question of a Substitution Account in accordance with Paragraph 6 of the Committee's communique of March 7, 1979. Such an Account, administered by the Fund, would accept deposits of U.S. dollars from members of the Fund and certain other official holders in exchange for an equivalent amount of SDR-denominated claims. In the light of the report submitted by the Executive Board, the Committee concluded that such an Account, if properly designed, could contribute to an improvement of the international monetary system and could constitute a step toward making the SDR the principal reserve asset in the system.

In order for the Account to achieve widespread participation on a voluntary basis and on a large scale, among other things, it should satisfy the needs of depositing



members, both developed and developing, its costs and benefits should be fairly shared among all parties concerned, and it should contain satisfactory provisions with respect to the liquidity of the claims, their rate of interest, and the preservation of their capital value.

The Committee, noting the progress that has been made and recognizing that a number of issues remain to be resolved, asked the Executive Board to continue to direct priority attention to designing a Substitution Account plan in accordance with the preceding paragraphs and in light of the views expressed by the members of the Committee, and to report progress to the next meeting of the Interim Committee.

VIII. The Committee agreed to hold its next meeting in Hamburg, Germany, on April 25, 1980.

IX. The Committee expressed their warm appreciation for the hospitality of the Government of Yugoslavia and for the excellent arrangements provided for the meeting.

**Exhibit 63.—Press release, October 16, 1979, concerning the requirement that future sales of Treasury gold be subject to variations in amounts and dates of offering**

The Department of the Treasury said today that future sales of Treasury gold will be subject to variations in amounts and dates of offering.

New standard bid forms for use in future auctions will be made available. Dates and amounts will not be specified in these bid forms, but would be the subject of Treasury announcement prior to an auction.

Under the new procedures, auctions can be held within a few days of an announcement and the amounts to be auctioned can be varied as may be appropriate at the time.

**Exhibit 64.—Remarks by Assistant Secretary Bergsten, November 13, 1979, before the World Affairs Council, Boston, Mass. entitled "The International Monetary System: Current Situation and Future Prospects"**

Just over a year ago, the United States dramatically adopted a series of measures to strengthen the dollar in the exchange markets. Over the last month, we have taken a series of further steps that complement and strengthen these efforts.

It is therefore useful to review the international monetary events of the past 12 months, with three key questions in mind:

- Has greater exchange rate stability been achieved?
- Is fundamental adjustment of the underlying imbalances taking place?
- Is the international monetary system working well enough, or are further improvements needed in its functioning?

There have certainly been disappointments during this period, which have set back our effort. Inflation has accelerated. The oil situation is having a major impact on prices, growth, and payments imbalances here and abroad. But I believe that major progress has also been made, and that too little attention has been paid to that progress:

- The dollar has strengthened, and exchange markets disorders have been curbed.
- The balance of payments adjustment process has operated almost precisely as the textbooks predict.
- Indeed, the impact of the oil price and supply situation has tended to mask the successful adjustment of the large imbalances of the United States, Germany, and Japan which had been the principal sources of exchange market instability in recent years.
- It is thus clear that the monetary system is working effectively, though we have during this period also seen the need for its further evolution—and begun to move in that direction.

## Exchange market developments

It may be useful to begin the review by recalling the exchange market situation last fall. Although the United States had already begun to make progress in reducing its record trade and current account deficits, confidence in our ability to achieve a sustainable position was being eroded by rising inflation and delays in implementing an energy program. Severe and persistent exchange market disorders developed which led to an excessive decline of the dollar. In the month of October, the dollar fell sharply against virtually all major currencies.

This excessive decline of the dollar added needlessly to inflation in our own economy. Because the dollar remains the world's key currency, this decline also threatened the stability of the entire international financial system. This, in turn, threatened our own economy because one of every eight manufacturing jobs in this country and 1 of every 3 acres of farm land produce for export, and because almost 1 of every 3 dollars of U.S. corporate profits derives from the international activities (investments as well as exports) of American firms.

Forceful, direct action was therefore required to break the psychological atmosphere, restore confidence and establish a basis for greater international financial stability. Our measures began in August 1978 with an intensified effort to control inflation; they included a series of steps on monetary policy and adoption of the wage/price guidelines. However, the individual steps, looked at in isolation, were seen as insufficient and even intensified the negative atmosphere.

On November 1, the United States announced a package of measures to strengthen the dollar at home and abroad. The package included a then unprecedented 1-percent increase in the discount rate and other measures to tighten monetary policy, expanded gold sales to improve the trade position and the mobilization of up to \$30 billion in foreign currency resources to finance the U.S. share of joint intervention operations—with Germany, Switzerland and Japan—in the foreign exchange market to restore stable conditions.

After an initial period of testing official intentions, the exchange markets calmed and the dollar experienced increasing demand throughout the first half of the year. Leads and lags returned to normal. Large net capital inflows to the United States developed as short positions were closed out.

However, despite the measures adopted in late 1978, our inflation rate continued to rise. As a result, market sentiment again turned bearish on the dollar. The concerns mounted irregularly but with rising force in September, and some movement occurred in the rates. Not all attention centered on the dollar, however. The German mark exhibited growing strength within the European Monetary System, which led to speculation on a realignment of rates there, but which also put additional pressure on the dollar.

Three factors helped bring this episode to a close: An EMS realignment, the October 6 actions by the Federal Reserve, and subsequent actions by the Treasury. Despite the periods of pressure, the dollar now stands substantially above the levels of last October. In terms of a trade-weighted average against the currencies of other major industrial countries, the dollar has increased in value by about 8 percent, including 35 percent against the Japanese yen and 3 percent in terms of the German mark.

The dollar is also about 8 to 12 percent higher in terms of the major currencies needed to pay for OPEC imports. (The precise figure depends on the averaging technique used.) Contrary to the widespread impression that it has weakened substantially since midyear, the dollar has strengthened by more than 2 percent in terms of an average of other major currencies since the June OPEC meeting. This point is extremely important, since a "weaker dollar" is sometimes cited as justification for increased oil prices. The reality is to the contrary.

The renewed strength of the dollar derives from a variety of sources. Clearly the measures of November 1, 1978, and our subsequent actions have demonstrated forcefully our determination to deal with exchange market disorders. We will continue to intervene actively in the foreign exchange market when conditions require, and have ample resources for this purpose. In this connection, Treasury has recently issued

\$1.1 billion equivalent of securities denominated in deutsche marks and plans a further offering of up to DM 2 billion in January.

We have also adopted a more flexible gold sales program to help deter the speculative disturbances in the gold market which have caused instability in other commodity markets and the exchange markets. In the future, sales of Treasury gold will be subject to variations in amounts and dates of offering, thereby increasing the uncertainties and risks associated with gold speculation. In accordance with this approach, 1.25 million ounces of gold were sold on November 1.

### The adjustment process

Exchange market intervention, and other efforts to deal with market forces directly, can of course succeed only if they rest on a solid underlying position. Indeed, we were able to move boldly in November 1978 because we were confident that the fundamental trends were moving in the right direction; and hindsight reveals that we were right, in that the U.S. external position had already begun to improve markedly after the first quarter of that year.

Indeed, substantial improvement has now been recorded in the U.S. current account position. Last November, we were projecting a halving of the U.S. current account deficit from \$14 billion in 1978 to the \$6-\$8 billion range in 1979, assuming no further increase in oil prices. In fact, oil prices have risen by more than 60 percent—a development which no one expected, and which has raised our 1979 oil bill by about \$16 billion.

Nevertheless, our current account deficit during the first half of this year was only \$1 billion. For the year as a whole, it is expected to run a few billion dollars at most. In 1980, we expect the United States to be in fairly substantial current account surplus, assuming oil prices rise no more than prices of other goods. Indeed, we expect the United States to have by far the largest current account surplus outside the OPEC group.

The improved U.S. performance derives from two key developments. First, the trade deficit in the first three quarters of 1979 is running at a \$6 billion annual rate below the \$34 billion deficit in 1978 despite the rise of \$16 billion in oil imports. Our nonoil trade balance has, in fact, improved by a whopping \$44 billion annual rate over the past six quarters.

In the year through September, the volume of nonagricultural exports is estimated to be more than 20 percent higher than the same period in 1978. At the same time, the volume of nonoil imports rose by only about 2 percent. Since the volume of world trade as a whole has been growing by 5 to 6 percent, it is apparent that both our export- and import-competing industries have made major gains in market share. The lagged effects of competitive gains from past exchange rate changes, and shifts in relative growth rates, have produced this substantial improvement in the competitive position of the United States. In 1980, these factors will produce continued improvement in our overall trade balance even though oil import costs will rise another \$10 billion or so, even on the basis of current prices.

Second, the United States surplus on services transactions is also growing rapidly. It is presently running about \$7 billion higher than the \$20 billion surplus achieved in 1978. Receipts from U.S. direct investment abroad have been especially strong, reflecting the improved profitability of foreign operations as growth overseas picked up and the translation effects of past exchange rate movements. In 1980, further gains in this area should result in an even larger services surplus.

It is worth noting that, at the present level of our services surplus, the United States can run a merchandise trade deficit of almost \$30 billion and still be in surplus on current account—the best single indicator of a country's international economic position. And our services surplus continues to rise rapidly each year. The structure of our current account is thus very different from that of Japan and Germany, each of which runs a sizable services deficit and thus must run a sizable surplus on merchandise trade to achieve overall current account balance.

In addition to the U.S. improvement, we are also witnessing a very significant adjustment in the positions of other major industrial countries. In particular, the Japanese position has reversed dramatically. A sizable Japanese deficit is expected for



1979, perhaps on the order of \$7–\$8 billion, in contrast to a \$16.5 billion surplus in 1978. Thus the Japanese position will swing by \$20–\$25 billion in 1 year alone. Moreover, Japan is likely to continue in deficit in 1980. The German surplus—which amounted to about \$9 billion in 1978—has been nearly eliminated this year, and a small deficit is likely next year.

These developments provide clear evidence that the international adjustment process works. To be sure, as we have known all along, there is a considerable delay between changes in relative prices and growth rates, on the one hand, and trade flows on the other. However, the results are now plain for all to see—just as they were, incidentally, after the exchange-rate realignments of the early 1970's. These adjustments will provide a pattern of payments balances among the major countries over the next year or so which will be a major factor for greater exchange market stability.

At the same time, it is obvious that even balanced current account positions are not enough to stabilize exchange markets unless there is a reasonable degree of confidence in the adequacy of economic policies in the major countries, and especially in the determination of the authorities in the United States to stand their ground until inflation is brought under control.

Food and energy prices have temporarily driven the increase in U.S. price indices into the double-digit range. In coming months, this pressure will recede as food prices moderate in the wake of good harvests and the OPEC actions work their way fully through the economy provided, of course, that there is no new surge in oil prices.

But the underlying inflation rate is still much too high and must be brought under control. The broad array of U.S. policies is directed at that objective. The recent Federal Reserve Board measures to restrain money supply growth are strong medicine and will be maintained. A disciplined fiscal policy will complement the Fed's efforts; indeed, the high employment budget has already swung more than \$30 billion toward restraint over the past 2 years. The National Accord between the administration and labor provides a basis for a more effective program of private sector wage/price moderation. But inflation has become deeply embedded in our economic structure, and will take a prolonged period of austerity to root out.

### **The evolution of the international monetary system**

The economic problems of the past decade have brought home forcefully to the United States the pervasive interdependence of national economies. Our autonomy in dealing with these problems is much less than many realize. Our real economic sovereignty is far less than our nominal sovereignty. The success of our efforts to bring inflation under control, achieve satisfactory growth and maintain a strong, stable dollar will be affected significantly by the actions of others.

The economic realities of interdependence have, however, out-paced the institutional mechanisms for dealing with them. Despite the progress cited above in adjusting national balance of payments positions, we are all too aware of the periodic outbreaks of instability in the monetary system and the frequent delays in initiating effective adjustment actions. We are still in the very early stages of the system of flexible exchange rates, and further improvements in its functioning are needed. The agenda for the 1980's must be directed toward developing a framework for ensuring that the international dimensions of economic policies are adequately reflected in national policy decisions.

The IMF Articles of Agreement provide a useful starting point in the critical areas of multilateral management of the global economy and international liquidity. While the new Articles provide wide leeway for members in the choice of exchange rate arrangements, they impose an obligation to foster economic stability and avoid unfair competitive exchange rate practices which, in a world of high inflation, may comprehend efforts to keep exchange rates artificially high just as a world preoccupied with excessive levels of unemployment faced periodic national efforts to keep exchange rates artificially low.

The IMF has been given enhanced responsibility for surveillance over the operation of the system to ensure that members fulfill these obligations. In the area of surveillance, the Fund has adopted principles for the guidance of members in conducting exchange rate policy, and procedures and criteria for assessing members'

policies. The guidelines, and IMF practice, recognize that surveillance must encompass the broad range of economic policies affecting balance of payments adjustment as well as exchange rate practices themselves.

The surveillance role constitutes a potentially major strengthening of the IMF's ability to promote a sound global economy. In the past, the Fund's ability to advise members and encourage appropriate policies was limited primarily to cases in which severe payments problems required a country to borrow from the Fund. The new provisions extend the Fund's mandate to countries which do not use its resources, including those in surplus or with alternative sources of financing. This more symmetrical approach should enhance the IMF's effectiveness.

The IMF has been understandably cautious in implementing this authority. But the time has come for it to take a more active role. Consequently, the United States has proposed several steps to strengthen IMF surveillance. These include procedures for measuring individual country performance against agreed global standards; requiring countries with large imbalances, surplus or deficit, to submit for IMF review an analysis of how they propose to deal with the imbalances; a more active role for the IMF Managing Director in initiating consultations with members; and establishment of a Governors Council with decisionmaking powers to replace the advisory Interim Committee. These steps could be an important start in developing an effective IMF role in managing the balance of payments adjustment process.

With greater interdependence among nations has also come a greater balance in terms of economic size. While the dollar remains the central currency for international reserves and liquidity, other currencies have an enhanced capacity for an international role. The development of a multiple currency system, however, would have an undesirable long-term potential for instability and disruption—as the opportunities for switching among currencies become even greater than today. Consequently, there is increased interest in multilateral efforts to manage global liquidity.

Interest has centered on efforts to promote the role of the SDR. The SDR was created in 1969 as a supplementary source of liquidity which did not rely on gold or payments deficits of the reserve currency country. The instabilities of the 1970's, with the rapid expansion of currency-based liquidity, retarded the full development of the SDR. However, the new IMF Articles establish the objective of making the SDR the principal reserve asset in the monetary system.

A number of important steps have been taken to promote the SDR. It has replaced gold as the central unit for the IMF, serving as the numeraire for the system and the unit of account and vehicle for many IMF transactions. Allocations of SDR's have been resumed, with SDR 4 billion being distributed annually during the 1979-81 period. The interest rate on the SDR has been brought more in line with market rates and the number of transactions in which SDR may be used have been expanded, thus improving the SDR's ability to compete with other reserve assets.

The IMF is now considering the establishment of a substitution account under which dollars and possibly other currencies could be exchanged for SDR denominated assets. The Interim Committee, at its recent meeting in Belgrade, concluded that a properly designed account could contribute to improving the system and promoting the role of the SDR, and requested a further report from the Fund's Executive Board next April.

The United States believes that the development of a substitution account could offer a number of attractions for the international community in general. The SDR is a diversified instrument, inherently involving less exchange risk than holdings of a single national currency. A substitution account could provide an internationally sanctioned, nondisruptive means for countries to achieve a desired reserve portfolio composition without having to hold a number of national currencies. Implementation of an account would constitute a significant step toward wider use of the SDR and to its longer term development as the principal reserve asset.

There are, however, many difficult questions in the construction of such an account and on sharing the costs associated with operating it. For example, questions must be answered concerning the interest rate and liquidity of the assets issued by the account, the investment of the dollar deposits and the amount and use of interest earnings, and measures to maintain the capital position of the account. These are exceedingly complex issues and we cannot be certain when, or whether, satisfactory answers will

be found. Nevertheless, the United States considers the effort worthwhile and is participating in a cooperative, constructive fashion.

### Conclusion

I draw the following conclusions from this assessment of international monetary developments over the past year, and of the current situation:

- First, a key source of the exchange market pressures and instabilities of recent years (the large U.S. deficit and the large German and Japanese surpluses) has disappeared. The pattern of payments balances among the major countries provides a sound basis for exchange market stability.
- Second, these changes demonstrate that the international adjustment process works. To improve the functioning of the process still further, however, it is essential to initiate corrective measures at an early stage before problems become self-reinforcing and require severe action—and the IMF may have a much larger role to play in that regard.
- Third, we should not be surprised—nor disturbed—if the relative role of the dollar in international finance tends to diminish over time. In lieu of a multiple currency system, which could be quite unstable, we might well see the gradual emergence of the SDR as a major factor in international finance.

Finally, it is clear that all solutions to our current problems require international responses. The mechanisms for cooperative action must be strengthened to provide for effective global management of the balance of payments adjustment process and the provision of international liquidity. We are living in an interdependent world, and our policies and institutions must be based on that reality.

### Exhibit 65.—Statement by Secretary Miller, March 10, 1980, before the Senate Committee on Foreign Relations, in support of S. 2271, legislation to strengthen the IMF and to provide for maintenance of the U.S. role in the IMF

Thank you for the opportunity to appear before the Committee in support of S.2271, legislation to strengthen the International Monetary Fund and to provide for maintenance of the U.S. role as the leader of this important institution.

We meet at a time of heightened international tension, affecting vital U.S. strategic and economic interests. Recent events have driven home dramatically the close interrelationship between foreign policy and economics. The turmoil in Southwest Asia has contributed to oil supply shortages and uncertainties and placed added strains on the international financial system. These developments have come at a time when the world economy is already facing extremely difficult problems. The massive oil price increases of the past year have led not only to slower growth and surging inflation but also to another period of dramatic changes in the balance of payments positions of the oil-importing countries. And today's world economic environment is likely to make it both more difficult for nations to obtain the financing needed to deal with their balance of payments problems, and more difficult for them to make the necessary adjustments to changed external circumstances.

The success of our efforts to deal with political tension and maintain peace in the 1980's will depend importantly on our ability to address current economic problems. The IMF is a cornerstone of U.S. international economic policy, providing the institutional framework for world monetary cooperation, finance and trade that is vital to the economic prosperity of the U.S. and the global economy. A strong and effective IMF is essential to our efforts to assure world monetary and financial stability and to provide the broad cooperative framework we will need to overcome fundamental economic difficulties.

The IMF serves two related functions: General guidance of the monetary system, and provision of temporary financing in support of members' efforts to overcome their balance of payments problems.

First, the IMF's Articles of Agreement constitute the operating rules of the international monetary system and establish member countries' obligations to promote



a cooperative and stable world monetary order. The decade of the seventies brought major changes in the international monetary system and in the IMF's role in guiding the system's operations.

In the area of balance of payments adjustment, the Bretton Woods par value exchange rate obligations have been replaced by obligations on members to pursue policies to achieve the underlying economic stability that is needed for genuine and sustained exchange rate stability. The IMF has been given the task of surveillance over members' compliance with those obligations, and over the operations of the balance of payments adjustment process more generally.

In the area of international liquidity the IMF membership has established the objective of making the special drawing right (SDR) the principal reserve asset in the international monetary system to help avoid the instabilities inherent in a system based on a multiplicity of national currencies.

These changes have paralleled and to a large extent reflected changes in the position and role of the dollar in the system. The original Bretton Woods arrangements assumed a fixed and central role for the dollar, with the U.S. position essentially passive and the product of other countries' actions in pursuing their own balance of payments policies and objectives. That arrangement ultimately became both unsustainable and intolerable in terms of U.S. economic interests. The new arrangements have provided much more scope for balance of payments adjustment by the United States, and recognize the need for greater symmetry in encouraging adjustment by all nations—those in surplus as well as those in deficit.

At the same time, the world's reserve system has been undergoing significant change. Increases in the relative economic size and financial capacity of other major countries have tended to bring some growing use of their currencies in international transactions and reserves. On the one hand, such a development could help to mitigate some of the burdens on the dollar and U.S. financial markets that arose from its extremely large international role. On the other hand, the process of change can itself be unsettling and disruptive, and there is a widespread view that increasing reliance on the SDR—an internationally created and managed reserve instrument—would be preferable to development of a full-scale multiple currency reserve system. The IMF over the past few years has taken a number of important steps to promote the role of the SDR and is presently considering a potentially significant further step in its examination of the substitution account.

The dollar nonetheless remains critically important to the operation of the international monetary system, and the U.S. economy remains a powerful element of that system. This will continue to be the case, and we recognize and accept the responsibilities incumbent on the United States to maintain a sound economic position and a stable dollar. At the same time, a strong IMF—able to encourage effective economic and balance of payments adjustment by all countries and able to guide the orderly evolution of the reserve system—is of direct and immediate importance to our economy and to our efforts to maintain the integrity and strength of the dollar.

The second basic function of the IMF, closely tied to its role in guiding the overall operation of the system, is the provision of temporary financing in support of members' efforts to deal with their balance of payments difficulties. Its aim is to encourage timely correction of balance of payments problems in a manner that is not destructive of national or international prosperity and thus to promote a smoothly functioning world payments system in the context of a strong and stable international economy. This is a central objective of the IMF and one in which all members must participate as an obligation of IMF membership.

It is important to understand the nature of IMF financing. The IMF is essentially a revolving fund of currencies provided by every member and available to every member for temporary balance of payments financing under prescribed criteria. Each country is obligated to provide its currency to the IMF to finance drawings by other countries facing balance of payments needs; and each country in turn has a right to draw upon the IMF in case of balance of payments need. When a country provides financing to the IMF; that is, when its currency is drawn from the Fund, it receives an automatic and unchallengeable right to draw that amount from the IMF in usable foreign exchange. This is the so-called reserve position in the IMF, an automatically

available reserve claim on the IMF which is normally carried in countries' international monetary reserves.

Financing thus flows back and forth through the IMF depending on balance of payments patterns and financing requirements at any given time. There is no set class or group of lenders or borrowers, no concept of "donor" or "recipient." All major industrial countries have drawn upon the IMF at times, and many members, developed and developing alike, have been both lenders and borrowers during the history of their participation in the IMF.

### Proposed increases in quotas

Throughout its history, the IMF has needed periodic increases in its quotas in response to the rapid growth of world economic activity and international trade and financial transactions. To maintain a strong IMF, capable of encouraging needed adjustment while providing the temporary financing required to maintain monetary stability, we must assure that its resources are adequate to meet potential demands. The proposed 50-percent general increase in IMF quotas is a key element in assuring that strength.

Quotas play a central role in the IMF. Members' quota subscriptions constitute the IMF's permanent financial resources. Quotas determine both the amount of IMF resources a member can draw when in balance of payments need, and its obligation to provide resources when its balance of payments is strong. Quotas determine the distribution of SDR allocations. And, of key importance in all IMF operations, quotas also determine voting power. Unlike the case in many institutions, where member countries try to hold down their shares of participation, in the IMF countries compete to gain the largest possible share of the total because of the votes and financing that a larger quota share provides. The United States has by far the largest IMF quota and thus the largest share of votes and potential access to IMF resources.

To ensure that IMF quotas remain realistic and adequate, they are reviewed periodically in relation to the growth of international transactions, the size of payments imbalances and financing needs, and world economic prospects. Such a review was initiated in 1977 and led to a resolution adopted by the IMF Board of Governors on December 11, 1978, with the U.S. Governor concurring, calling for an increase in overall IMF quotas by 50 percent, raising total quotas from about SDR 39 billion to roughly SDR 58 billion. The increase proposed for the U.S. quota amounts to SDR 4,202.5 million, equivalent to about \$5.4 billion at current exchange rates. This increase would raise the U.S. quota by 50 percent from SDR 8,405 million (or about \$10.9 billion) to SDR 12,607.5 million (or about \$16.3 billion).

The negotiation of quota shares is always difficult with pressures on the U.S. to accept a smaller quota share. Given the key roles of the dollar and the U.S. economy in the international monetary system, and the IMF's central role in guiding the operations and evolution of the system, it is essential that the U.S. maintain an appropriate share of quotas and votes, and thus its influence over basic decisions about the system. In the end, the pressures for a reduced U.S. share were successfully resisted during the most recent review, and only a very few selective changes in quota shares, all within the LDC group, were agreed.

The decision to propose a 50-percent overall increase in quotas reflected a widely felt view that quotas had, by any measure, failed to keep pace with potential balance of payments financing needs. Despite quota increases on four occasions during the IMF's history, aggregate quotas had fallen to about 4 percent of annual world imports in comparison with 8 to 12 percent during the 1960's and 10 to 14 percent during the 1950's. The adequacy of quotas had eroded particularly during the seventies, as the ratio of quotas to members' aggregate deficits fell by two-thirds between 1971-73 and 1978. In mid-1978 the Fund's usable quota resources—that is, its holdings of the currencies of members then in strong payments positions—totaled only about SDR 16 billion, or just over 1 percent of world imports. In November 1978, before the Supplementary Financing Facility was put in place, the amount of usable quota resources was effectively halved to around SDR 8 billion when the U.S. drew the equivalent of \$3 billion and the dollar was taken off the IMF's "budget" of currencies used in financing current drawings.



These shifts in the IMF's "liquidity" illustrate the difficulties of projecting either the level of usable IMF resources or the level of future drawings on the Fund. In its 1977 quota review, the IMF estimated that the level of international transactions between 1978 and 1983 would increase by 60 percent in SDR terms. In fact, that 60-percent figure is now much too low, as inflation, oil price increases, and other factors have caused a much more rapid expansion in the value of world trade and financial transactions. And even if we could accurately predict future levels of world trade, we would not know the pattern of trade, the size and distribution of payments imbalances, or the availability of financing from banks and other sources.

In determining how large a quota increase would be needed, it was recognized that the IMF's Supplementary Financing Facility, introduced last year to provide badly needed resources to the IMF on a temporary basis, would be phased out after a 2- to 3-year period. That facility was proposed and is regarded as a bridging operation to be followed by an increase in the IMF's permanent resources.

It was in the light of these considerations that the IMF membership concluded that a 50-percent increase in total quotas would be the minimum required to assure that the IMF remained in a strong position to meet prospective needs. Even a 50-percent increase will do little more than slow the decline in the relative size of IMF resources into the mid-1980's. In fact, most developing countries and some OECD members, fearing growing world economic uncertainties, pressed hard for a much larger increase.

Events since completion of the quota review have strengthened the justification for the quota increase. Oil market developments have again radically altered economic prospects and have drawn the world into a pattern of payments imbalances reminiscent of that following the 1973-74 oil price increase. Countries must, and will, begin adjusting to these developments, and that will cause further changes in world balance of payments patterns and financing needs that cannot be foreseen. Moreover, events in Iran and Afghanistan have created a climate of concern and uncertainty that makes it all the more important to have in place the institutional means for assuring monetary stability and for providing advice and financial support to countries facing the growing economic and financial problems of the 1980's.

At present, the IMF has usable quota resources estimated at about SDR 10 billion, plus SDR's held by the IMF totaling approximately SDR 1.1 billion. These resources are supplemented by amounts remaining available under the General Arrangements to Borrow equal to SDR 5.7 billion, and SDR 7.4 billion under the Supplementary Financing Facility which is scheduled to end in early 1981 or 1982.

Severe payments imbalances and consequent financing needs will very likely intensify during the next several years. At present, in broad terms, we anticipate an OPEC current account surplus of about \$120 billion in 1980 and current account deficits, after official transfers, of about \$70 and \$50 billion for the OECD and LDC group respectively. A world environment of slower growth, high inflation, heightened caution in the private financial sector, and the continuing threat of energy supply disruptions will simultaneously make the financing of external deficits and the adjustment of national economies to reduce those deficits more difficult.

The private financial sector will again be called upon to meet the bulk of expanding international financing needs, and we believe that the private banking system, including the U.S. banks, can and will continue to participate in the recycling process without incurring undue risk. At the same time, our regulatory authorities will be monitoring developments closely to help insure that the banks' loans are sound and that excessive concentrations do not arise. Moreover, flows of official development assistance will continue to rise. But we have to anticipate that a number of countries, developed and developing, will encounter growing financial difficulties, and pressures to adjust and bring their external positions closer into line with sustainable flows of financing. This will result in increased demands for official balance of payments financing, and early in 1980, the IMF is already processing requests for balance of payments financing that far exceed the total drawn in 1979 as a whole.

The IMF must have adequate resources—and this means adequate quotas—to encourage countries to adjust in an appropriate way, rather than adopt trade and capital restrictions, aggressive exchange rate policies, or unduly restrictive domestic measures in order to reduce their financing needs. Such restrictive measures could



have serious implications for the entire world economy and the prosperity of all nations, as well as for the economy of the country introducing them. We must not forget the lessons of the 1930's, when serious economic troubles were worsened by ultimately self-defeating actions of nations trying individually to preserve employment and prosperity during times of economic distress and international tension. The impact on the United States today could be especially harmful. Our economy has grown heavily reliant on world trade and financial flows. An interdependent world brings real economic benefits, but also greater vulnerability to outside developments. Imported goods, from raw materials to high technology products, are integrated into all phases of U.S. economic activity. Export markets constitute a major source of demand for U.S. goods and services. One out of every seven U.S. manufacturing jobs and 1 out of every 3 acres of U.S. agricultural land produce for export. For the U.S. economy specifically and the world economy generally, prosperity is dependent on a well-functioning international financial system.

Uncertainties about the magnitude, distribution, and financing of payments imbalances over the next few years make it impossible to project the precise level of IMF resources that will be used during the next 5 years. But we must assure ourselves that the IMF's resources are sufficient to enable it to meet its important responsibilities—sufficient as measured against historic standards and current trends, and sufficient against a realistic appreciation of the dangers we face as we enter a new decade.

### **The IMF and national balance of payments adjustment programs**

Let me turn, Mr. Chairman, to the IMF's role in fostering balance of payments adjustment on the part of its member countries. This is an area that has drawn a great deal of public attention in recent years, and one in which the IMF is again likely to become quite heavily involved as its members address the difficult problems they now face.

In trying to gain an understanding of the appropriate role for the IMF, it is important to bear in mind the purpose for which it provides financing: to help members overcome their balance of payments problems without recourse to measures destructive of national or international prosperity.

Access to IMF financing is contingent upon the member meeting certain criteria which are designed to ensure that the IMF's financial resources are used in a manner consistent with this purpose. In the initial stages of a member's use of IMF financing, the requirement is simply that the member have a balance of payments need. As a member makes greater use of regular Fund resources, it must demonstrate that it is making "reasonable efforts" to overcome its balance of payments difficulties. And if there is a need for further financing from the Fund—and the member begins to enter into the higher stages of its access to Fund resources—the IMF requires that a comprehensive adjustment program be developed by the member that provides "substantial justification" in terms of correcting the country's balance of payment problems. Such programs generally involve the use of certain "performance criteria" which establish concrete policy objectives and which are used at regular intervals during the program as indicators of the progress being made toward those objectives. This progression of policy requirements is what is referred to as Fund "conditionality."

It is generally agreed that the conditionality attached to IMF lending is essential to achievement of the IMF's purposes. Whatever the cause of a country's balance of payments problem, unless it is temporary and self-reversing, the country will ultimately have to adjust—it cannot indefinitely spend reserves and borrow abroad. Restrictions on trade and on exchange transactions may provide temporary relief, but can lead to retaliation from abroad and to pervasive distortions in the economy which often compound the member's economic problems. If policy adjustments are delayed too long, the country's creditworthiness and ability to borrow abroad will inevitably decline; trade credit will evaporate; investment and productivity will generally fall; and growth will decline or become negative. This in itself is one form of adjustment, but it is a harsh and inefficient adjustment. What may look like the easy way out is in fact very costly.

Most governments will make policy adjustments before the situation deteriorates to that extreme, but sometimes a country will not approach the Fund until the situation is desperate. This is a key point to remember. The Fund does not *cause* the lack of foreign exchange that interrupts vitally needed imports. Indeed the IMF, oftentimes alone, tries to help by providing resources to maintain the economy and balance of payments temporarily, and by providing policy advice that will help the borrower restore sustained economic stability and growth. In return for this financing, the world community expects the government to forswear measures disruptive to the world economy. To assure repayment and the most beneficial results for the country, the Fund requires that the member undertake appropriate measures to solve its balance of payments problem. But barring a major change in the country's economy such as discovery of oil or a political decision by other nations to finance the deficits of the country, on a more or less *permanent* basis, every nation will have to adjust. In most cases the sooner needed adjustments can be initiated the better since the longer adjustment is delayed, the more difficult and painful it will be.

Quite often, the adjustments that must be made require difficult policy choices for the country concerned and can involve short-term restraint and hardship affecting virtually all segments of the population. The immediate difficulties of a relatively short-term restraint program must be weighed, however, against the pervasive, destructive—and lasting—effects of an inflation that is allowed to go unchecked on investment, employment, development, and general welfare. If the IMF can help a country to restore a sound basis for growth and development through implementation of an adjustment program, then the longer term benefits, economic and social, can far outweigh the shorter term costs.

This does not mean that the IMF should take a rigid or doctrinaire approach in dealing with its members. Indeed, it is widely overlooked that the institution has, in fact, adapted its policies and practices and taken a large number of steps to improve its effectiveness and ability to respond to members' changing needs.

First, reflecting the generally increased scale and persistence of balance of payments problems, the IMF now provides more financing for longer periods for nations with adjustment problems. Quota limits on drawings have been expanded; and for drawings with higher conditionality, in the upper credit tranches, 2- and 3-year programs have become much more the accepted rule, in contrast to the 1-year program that was traditional in earlier days.

In addition, a variety of IMF facilities are now available to members, ranging from unconditional reserve tranche drawings through facilities such as the Compensatory Financing Facility and the first credit tranche (both with relatively "light" conditionality requirements) to the upper credit tranche and Extended Fund Facility drawings. Of total drawings amounting to nearly \$30 billion since 1973, roughly two-thirds has been drawn from unconditional or relatively unconditional facilities. Some countries have, of course, gotten into more serious difficulty and have had to turn to the more conditional facilities—which have themselves been expanded and adapted—and these are the cases one hears about most often. But it is important to bear in mind the whole spectrum of IMF financing facilities when assessing its role in balance of payments financing and adjustment.

Second, the IMF has undertaken a major review of conditionality in the upper credit tranches and has established a new set of guidelines for its application. To an extent, these new guidelines formalize certain protections for borrowing countries that had already existed in practice, but they also add important new features. For example, they now emphasize the desirability of encouraging countries to adopt corrective measures at an early stage, before very severe adjustment problems arise, and recognize the need for more gradual and more flexible adjustment over longer periods. They also recognize that adjustment measures frequently encompass sensitive areas of national policy, and provide that in helping to devise adjustment programs the Fund will pay due regard to the concerns of governments about the compatibility of such programs with their domestic social and political objectives and economic priorities. They provide that "performance criteria" will normally be confined to macroeconomic variables (other than those performance criteria needed to implement specific provisions of the Articles such as the avoidance of exchange restrictions). The new guidelines should help dispel the idea that conditionality is a weapon for imposing

unnecessary hardship and make clear that for countries with severe imbalances, the adequate and timely adjustment which is the objective of IMF conditionality is in the best interests of both the individual country involved and the world community.

A third change in the IMF's approach to adjustment, and a particularly important one, is one that I mentioned earlier: its new role in surveillance. Surveillance over every IMF member's efforts to foster orderly underlying economic and financial conditions provides valuable IMF leverage for promoting sound adjustment policies by all countries, surplus or deficit, whether or not they draw on the IMF's resources. It is designed to introduce a badly needed symmetry in the international monetary system, more effectively encouraging adjustment efforts by surplus countries, and not leaving the entire burden of adjustment on deficit countries. Development of IMF surveillance can be helpful in various ways. To the extent it encourages earlier adjustment action, it helps to avoid the more severe corrective measures which become necessary as a country's situation worsens; and to the extent it encourages adjustment action by all countries with large imbalances, it reduces the relative emphasis on those deficit countries drawing upon the IMF.

Thus the IMF is making a continuing effort to adapt to the changing needs and circumstances of its members. This process should, and will, continue. But as we move to adapt IMF policies and practices, we need to keep the IMF's basic purposes clearly in view, and ensure that its programs do, in fact, effectively promote adjustment by its members. This is in the individual borrower's own interests and of the international community as well.

### **Budgetary treatment of IMF quota increase**

Before I conclude, Mr. Chairman, let me briefly mention the question of the budget and appropriations treatment of this quota increase. The President's budget proposes that a program ceiling on the increase be provided in an appropriations act. We have been consulting closely on this question with interested committees, and considerable interest has developed in an alternative approach which would involve the following elements:

- Appropriations would be required in the full amount of the increase, and that sum would be included in budget authority totals for fiscal year 1981.
- Payment of the quota increase by the United States would result in budgetary outlays only as cash transfers are actually made to the IMF on the U.S. quota obligation (25 percent of our quota increase will be transferred immediately in the form of SDR's; subsequent transfers can occur when dollars are needed by the IMF in its operations).
- Simultaneously with any cash transfer under the quota subscription, an offsetting budgetary receipt, representing an increase in the U.S. reserve position in the IMF, would be recorded.
- As a consequence of these offsetting transactions, therefore, transfers to and from the IMF under the quota obligations would not result in net outlays or receipts.
- Net outlays or receipts resulting from exchange rate fluctuations in the dollar value of the SDR-denominated U.S. reserve position in the Fund would be reflected in the Federal budget. These net changes cannot be projected and thus would be recorded only in actual budget results for the prior year.

We are continuing our consultations on this matter. The point I would stress today is that under either the program ceiling contained in the President's budget or this alternative approach, U.S. payments on its quota subscription would not affect net budget outlays or, therefore, the Federal budget deficit.

### **Conclusion**

Mr. Chairman, the proposed quota increase is important for three reasons.

First, from the point of view of the international monetary system as a whole, it will help assure that the IMF can continue to meet its responsibilities for international monetary stability in a period of strain, danger, and financial uncertainty.



*Second*, from the point of view of individual countries, it will provide additional resources to encourage cooperative balance of payments adjustment policies; and I note that IMF resources have been of major direct benefit to the United States when we faced severe balance of payments pressures.

*Third*, from the point of view of the United States, it maintains our financial rights and our voting share in the institution during a time when far-reaching changes in the monetary system—for example, a substitution account—may be under consideration.

The record of the IMF is a good one in adapting to changing world circumstances and responding to the needs of its members. The proposed quota increase will provide the Fund with resources needed for its valuable work, and I urge the Committee to approve this legislation.

**Exhibit 66.—Communique of the Interim Committee of the Board of Governors of the International Monetary Fund on the International Monetary System, April 25, 1980, issued after its 14th meeting in Hamburg, Germany**

1. The Interim Committee of the Board of Governors of the International Monetary Fund held its fourteenth meeting in Hamburg, Germany, on April 25, 1980 under the chairmanship of Mr. Filippo Maria Pandolfi, Minister of the Treasury of Italy. Mr. Jacques de Larosiere, Managing Director of the International Monetary Fund, participated in the meeting. The following observers attended during the Committee's discussions: Mr. G. A. Arsenis, Director of Money, Finance and Development Division, UNCTAD; Mr. Alexandre Lamfufussy, Economic Adviser and Head of the Monetary and Economic Department, BIS; Mr. Pierre Languetin, Member of the Governing Board, Swiss National Bank; Mr. Emile Van Lennep, Secretary-General, OECD; Mr. Olivier Long, Director General, GATT; Mr. Rene G. Ortiz, Secretary-General, OPEC; Mr. Francois Xavier Ortoli, Vice-President, CEC; Mr. Jean Ripert, Under-Secretary-General for International Economic and Social Affairs, UN; Mr. Ernest Stern, Vice President, Operational Staff, IBRD; Mr. Cesar E. A. Virata, Chairman, Development Committee.

2. The Committee discussed the world economic outlook and the policies appropriate in the current situation. Two aspects particularly concerned the Committee: world-wide inflation and the payments imbalances of the non-oil developing countries.

Expressing great concern at the dramatic and widespread rise in rates of inflation since its meeting in Belgrade, the Committee agreed that the top priority being given in many countries to the fight against inflation must not be relaxed.

The Committee recognized that short-term prospects for growth of the world economy, and particularly of economic activity in the industrial countries, are not good. Success in reducing inflation was considered a condition for better investment performance and resumption of satisfactory growth over the longer term.

It was recognized that efforts to contain inflation require an appropriate balance between monetary and fiscal policies. In that light the Committee stressed that more effective use of fiscal policy, with better control of government spending, is essential.

The Committee continued to attach great importance to avoiding secondary repercussions of the recent oil price increases on wages, other incomes, and prices of non-oil goods and services. The Committee noted the desirability of doing everything feasible to ensure that incomes grow at a rate which is consistent with anti-inflationary policies.

The Committee also emphasized the need to supplement fiscal and monetary policies with measures designed to improve supply conditions and promote higher levels of saving and investment. In this general context, the Committee recognized the pervasive impact of the energy situation on all aspects of economic performance and stressed the importance of measures to conserve energy and to develop new sources of energy.

With respect to the international payments situation, the Committee noted that shifts in current account balances among major groups of countries are proving even larger than was visualized at its previous meeting last October. According to the estimates of the IMF staff, the current account surplus of the oil exporting countries is now

expected to reach \$115 billion in 1980 and to remain very large in 1981, while the combined current account deficit of the non-oil developing countries is likely to approach \$70 billion in 1980—compared with \$55 billion in 1979—and to rise still further in 1981, and the deficit of the industrial countries on current account (excluding official transfers) will probably rise from \$10 billion in 1979 to the range of \$45-\$50 billion in 1980 before subsiding in 1981.

What the Committee found most disturbing about the payments imbalances now in prospect was the sharp increase in the current account deficit of the non-oil developing countries. It was feared that this adverse swing would generate external financial difficulties for many of these countries, and that a number of low-income countries in the group would face severe problems in maintaining an adequate flow of imports. To avert hardships for these latter countries, the Committee urged provision of sufficiently large amounts of aid and concessional loans.

The Committee noted that a number of developing countries, and especially those whose own manufacturing industry is most advanced, have relatively good access to international financial markets, and may be expected to cope with the sharp rise in their import bills partly through expanded international borrowing. While recognizing the need for prudential supervision, the Committee expressed concern that such supervision should not impede recycling. The Committee was concerned, nevertheless, about the medium-term implications of such heavier borrowing. With the escalation of outstanding debt, amortization payments and interest costs—especially those incurred on fixed terms involving high rates of interest—will make sizable claims on debtors' export earnings and other available funds over the next few years. To minimize these burdens, the Committee urged that developing countries seek a judicious blend of adjustment and financing to meet the payments problems immediately ahead.

Recognizing that the ability of non-oil developing countries to achieve the desired objectives would depend importantly on their access to foreign markets, the Committee urged the industrial countries to keep their markets open to exports from developing countries. Avoidance of protectionist trading policies was considered of vital importance at a time of sluggish growth in world economic activity.

3. In view of the outlook for the world economy and, in particular, the prospect of large and widespread payments imbalances, the Committee agreed that the Fund should stand ready to play a growing role in the adjustment and financing of these imbalances. In this connection, the Committee endorsed the views set forth in the Managing Director's statement on the subject and agreed with him that any such financing by the Fund should be made available in conjunction with adjustment policies appropriate to the needs and problems of members in the present economic situation.

The Committee recognized that, in view of the availability of funds under the supplementary financing facility and the expected increase in quotas under the Seventh General Review, the Fund is, under present circumstances, in a relatively liquid position. Nevertheless, in the light of the size and the distribution of payments imbalances, the necessity to phase adjustment over a reasonable period of time, and the time needed for the completion of any borrowing arrangements, the Committee encouraged the Managing Director to start discussions with potential lenders on the terms and conditions under which the Fund could borrow funds to increase its resources, if and when the need arises.

The Committee believed that, in addition to any action by the Fund, additional development assistance would need to be provided to the low income countries that are most severely affected by the present situation and, in this connection, it endorsed the view expressed by the Development Committee on the need for such assistance. The Committee requested the Managing Director and the Executive Board to start examining in depth the relevant recommendations of the program of immediate action of the Group of 24, in light of the press communique of the Ministers of the Group of 24, with a view toward a substantive discussion next September.

4. The Committee expressed concern at the fact that, although the Resolution of the Board of Governors on the Seventh General Review of Quotas had been approved nearly one and a half years ago, the quota increases of SDR 19.6 billion approved under it had not yet come into effect. The implementation of these increases would

enhance the ability of the Fund to serve the needs of its members in the difficult payments situation ahead. The Committee stressed again the importance of an early implementation of these increases and urged those members that had not yet consented to the increases in their quotas to do so as soon as possible, so that the increases could become effective in the course of 1980.

5. The Committee noted that the present gold sales program, which is nearing completion, has yielded a very large amount of resources for the benefit of the developing countries—about SDR 3.9 billion—the greater part of which was used for balance of payments assistance on concessionary terms to the low income developing countries. The Committee asked the Executive Board to study the future of the Trust Fund. This study should encompass, inter alia, the possibility of using a part of the Trust Fund repayments for ameliorating the conditions of loans to low income developing countries.

The Fund should also explore the possibility of obtaining other resources to subsidize its lending to low income developing countries.

6. The Committee commended the Executive Board for the progress it had made in designing a plan for a substitution account along the lines requested by the Committee in its communique issued in Belgrade. The Committee noted that the Board had reached, in Part II of its report, provisional agreement on a wide range of features of such an account. The Committee also noted that some issues remained to be solved, including arrangements for the maintenance of financial balance in the account. The Committee, after a discussion of these issues, expressed its intention to continue its work on this subject.

7. The Committee noted with satisfaction the steps taken to widen the uses of SDRs and welcomed the decisions taken by the Executive Board under which SDRs can now also be used in swaps, forward operations, and in making donations. The Committee also welcomed the recent decisions under which an increased number of official institutions can hold and deal in SDRs.

The Committee noted that the Executive Board had conducted an examination of the SDR valuation and interest rate baskets with a view to simplifying and enhancing further the attractiveness of the SDR. The Committee endorsed these objectives and generally expressed the view that it would be desirable for the interest and valuation baskets to be identical. The Committee asked the Executive Board to examine the matter further and to take the necessary action.

8. The Committee agreed to hold its next meeting in Washington, D.C. on Sunday, September 28, 1980. The Committee also agreed to hold a meeting in Libreville, Gabon, in the spring of 1981.

9. The Committee expressed its warm appreciation to the Government of the Federal Republic of Germany and to the Free and Hanseatic City and the people of Hamburg for their hospitality and for the excellent arrangements provided for the meeting.

**Exhibit 67.—Remarks by Secretary Miller, June 4, 1980, before the International Monetary Conference, New Orleans, La., regarding challenges in the world economic and monetary system in the 1980's**

Since I became Secretary of the Treasury last August, I've been looking forward to the opportunity to participate in the International Monetary Conference. I consider it part of my coming of age as Secretary.

Last evening, when I left Washington, the radar system was knocked out and airplanes were delayed and cancelled. I thought that perhaps Divine Providence was interfering to see that I did not participate in this conference. Four hours later, when we made new connections to fly into New Orleans, I found myself on the same plane as Paul Volcker. I then realized it was merely Divine Providence making sure I was in good company.

Over the past 10 years, my predecessors as Secretary have addressed this Conference under circumstances that have involved rapid and unprecedented changes which have indelibly altered the world economic and monetary system.



The process of change continues, and today I would like to chat with you about some of the challenges we face in the 1980's.

The problems confronting the world economy today are even more basic than those during reconstruction following World War II. As bankers, you are and will be in the thick of things. Your view of the future, your lending decisions, your reaction to changes in the world environment will all play a major role in our success or failure in meeting the tests that lie ahead.

Many of our problems have their roots in world economic developments of the 1970's. The past decade was disturbing in several respects. The seventies represented a sharp break from the past, ushering out the post-war period of steady global recovery and expansion. The world economy reached a turning point in 1973. The strong world expansion from late 1969 into the early seventies produced a highly synchronized, but unsustainable, upswing in 1972-73. Surging demand led to a worldwide inventory buildup. Commodity prices rose dramatically, particularly for energy.

Improving living standards and rising industrial production brought huge increases in energy demands over the post-war years, with oil consumption far in the lead. The level of U.S. domestic oil production peaked out. OPEC nations responded to the new situation by raising prices. At the beginning of the 1970's, a barrel of OPEC oil cost about \$2.00. As we enter the 1980's, the price has increased sixteenfold, playing havoc with the world economy.

The powerful inflationary and growth-depressing impact of rising energy prices was augmented by declining productivity growth over the last decade. This was accompanied by a proliferation of government regulations, and more and more general and specific interference with the private market system. As underlying inflation rates rose dramatically, so did inflationary expectations. This produced the classic effect—a flight by consumers and businesses from money into goods.

One consequence has been a reduction in average savings rates in many countries. Inflation has also affected the level of real capital investment so that productive stock has not grown as rapidly as the labor base. In the wake of sharp energy cost increases, the existing capital stock has become increasingly outmoded. At the same time, increases in unemployment have led to larger government transfer payments, larger expenditures, and heavier pressures on budgets.

All this has taken its toll on our economies. It has produced major structural problems that need to be addressed forcefully in the years ahead.

In particular, the share of GNP devoted to investment needs to be increased. For this to happen, the hard fact is that either the government share or the consumer share must decline.

The buffeting experienced by the world economy during the past decade has been traumatic for governments, for labor, for business, and for consumers—in developed and developing countries alike. We have all suffered from the shock; we can also learn from it. The main lesson is that progress lies in successful adaptation.

We need to adapt our ways of thinking, our policies, our institutions, our economic relationships, and the very structures of our economies. All nations have the responsibility to the international community—and to themselves—to contribute to the needed adjustments. The United States and other oil-importing nations have the responsibility to reduce their excessive reliance on imported oil, to bring inflation under firm control, and to create an environment for renewed investment and productivity growth. The oil-exporting nations have an obligation to contribute to orderly economic and financial adaptation through responsible production, pricing, and investment decisions. Both the private and the international financial institutions have major roles to play in the entire process.

### **The U.S. responsibility**

The problems facing the U.S. economy closely parallel those of other oil-importing countries.

Foremost among these is a destructive and intolerable rate of inflation. Inflation has built up over some 15 years, and its roots are now deeply imbedded. Success in the battle against inflation requires a comprehensive, integrated strategy to reduce its fundamental causes, not just to treat its symptoms. This is our first priority.

Overcoming inflation represents by far the most important contribution the United States can make to assuring a stronger world economy.

The primary weapons in our war against inflation are fiscal and monetary discipline, an effective pay and price policy, a vigorous program to reduce reliance on imported oil, regulatory reform, increased investment, productivity improvement, and a sound and stable dollar.

*Fiscal policy.*—In order to reduce inflation and release resources to address structural problems, we are directing major efforts toward bringing Federal spending under more effective control. Prudent economic management requires that the Federal budget be balanced over the business cycle.

If approved by Congress, the budget President Carter submitted as part of his March 14 intensified anti-inflation program would be the first balanced budget in 12 years.

Together with measures to control Federal on- and off-budget credit demands, the achievement of budget balance over the business cycle will have a major impact on credit markets and on inflation and inflationary expectations.

*Monetary policy.*—A second weapon in the war against inflation is a disciplined monetary policy. The Federal Reserve has held a tight control over the growth of the money supply in order to starve out inflation. This has contributed to a growing confidence in financial and other markets.

While monetary policy has been effective, the growing threat from inflation prompted President Carter to undertake strong additional steps to control credit. These new, temporary measures, in conjunction with continued monetary restraint, accomplished their purpose. They were designed to arrest the unproductive use of credit that was prevalent earlier in the year, and to deflate the inflationary bubble of expectations that had contributed to the excessive credit spending and speculation.

Credit and financial markets are now operating in an orderly and efficient manner. Interest rates have come down sharply from earlier peaks. We seem to have broken the back of inflationary expectations *for now*. This has already made it possible to relax the temporary controls somewhat.

As the Federal Reserve has already indicated, it is firmly committed to its basic monetary policy and determined to maintain the growth rate of the monetary aggregate within its established target ranges. This is certainly the proper course to ensure progress in the war against inflation.

*Pay and price policy.*—Fiscal and monetary restraints represent powerful weapons to attack the fundamental causes of inflation. But these policies work slowly. Therefore, we need a “bridging” technique to help avoid a vicious wage-price spiral until fiscal and monetary measures take hold. This is the purpose of the voluntary program to moderate pay and price increases. With the mutual cooperation of business and labor, overall price and pay increases have been smaller than otherwise would have been the case. This has been very helpful in avoiding a ratcheting-up of inflation.

*Government regulation.*—In battling inflation, we do not intend to overlook the cost-raising actions of government. Among these are the unnecessary regulations that could not pass a fair assessment of their costs and benefits. Much of the regulation of airlines, trucking, railroads, banking, and communications industries, as well as some environmental, safety, and trade regulations, and a generally heavy burden of imposed paperwork, have created inefficiencies, distortions, and excessive costs that feed through our economy and push up prices. The administration is intensifying its efforts, through legislative proposals and administrative processes, to remove unnecessary regulations and to improve the quality of desirable regulations. The result will be a reduction in the overall burden of government.

*A stable dollar.*—Policies to control inflation help to strengthen the dollar. In turn, a sound and stable dollar is essential if we are to achieve price stability. The two are mutually reinforcing. Moving forcefully to assure better control over the expansion of money and credit and to help curb excesses in commodity and other markets will dampen inflationary forces and inflationary expectations, and contribute to greater stability in foreign exchange markets.

The dollar has strengthened over the period since the President’s November 1, 1978, announcement of a major U.S. exchange market program. We have and will continue

to deal forcefully with unwarranted exchange market pressures in order to maintain a sound and stable dollar.

*Energy policy.*—The tenfold increase in world oil prices has been a principal contributor to the acceleration of inflation since 1973. Oil price increases have had no less an effect in the first year of the 1980's. To win the war against inflation, it is absolutely essential that the United States reduce its dependence upon imported oil and upon oil itself as a source of energy. It is essential to our national security that we gain control over our own destiny and that we move to do so with all possible speed.

To achieve these objectives, President Carter has proposed a broad and comprehensive energy program, including: Decontrol of oil prices, a limit on oil imports, energy conservation, increased development and use of conventional domestic sources of energy, increased use of renewable energy sources and the development of unconventional domestic energy supplies, and a windfall profits tax to allocate the increased revenues generated by decontrol of domestic oil prices. The latest element in this program is the President's proposal for a 10-cent gasoline conservation fee.

There can be no question that our national and economic security is threatened by dependence on oil imports. The 1979 oil price explosion was the primary cause of the acceleration in inflation, the swift escalation of interest rates, and the massive drain of purchasing power, all of which have combined to help throw the U.S. economy into reverse gear.

Since 1970, we have seen our oil import bill rise from \$3 billion to \$90 billion. A failure to stem oil imports would have serious consequences for our efforts to achieve lasting improvement in the U.S. balance of payments and to maintain a stable dollar, and would threaten our efforts to solve our domestic inflation problem.

Low gasoline prices are a major cause of our over-consumption of imported oil. The gasoline conservation fee introduced by President Carter is a moderate but straightforward step toward reducing our dependence on foreign oil. By the end of the first year, it would reduce oil imports by 100,000 barrels a day, and by the end of the third year, it would reduce oil imports by up to 250,000 barrels a day, producing a balance of payments savings of more than \$3 billion. The fee would produce additional demand restraint and demonstrate the willingness of the United States to make sacrifices to curtail gasoline use. This would be an important element in securing the international cooperation that is vital if we are to bring the oil price explosion under control. As you know the fee is under challenge in both the courts and in Congress. President Carter is making a courageous, all-out effort to retain it as an instrument of U.S. energy policy. The fight to achieve a rational U.S. energy policy has been long and hard and slow. No doubt there will be setbacks and detours ahead, as there have been in the past. But we have made considerable progress, and we intend to achieve even more.

We have already started to see results from earlier conservation efforts. During the first quarter of 1980, U.S. oil consumption was 9.4 percent below the same period last year. This sharp reduction reflected consumer reactions to higher prices and increased efficiency. It was mirrored in our demands for oil imports which in the first quarter fell 12.4 percent from a year earlier. Data on total energy use also confirm our increased efficiency. Between 1974 and 1978, the ratio of energy consumption per unit of industrial output decreased about 20 percent. Between 1972 and 1979, energy consumption per dollar of GNP fell roughly 10 percent. The direction is right, but we need to follow through by putting our program fully into place.

*Investment.*—Finally, if we are going to control and reduce the underlying rate of domestic inflation, we will need a very substantially higher level of investment. This means we will need to devote a larger share of our output to investment and less to consumption. Investment, of course, begins with savings. But inflation until now has generally discouraged savings. It has also dampened investment by increasing uncertainty and the risk involved.

After we have displayed the willingness and fortitude to bring our Federal spending under control, we can and should provide the incentives that will encourage savings, investments, and productivity that are so essential to economic progress with price stability.



### Overall responsibility of the oil-importing nations

The problems of energy and intense inflationary pressures, of course, also confront other oil-importing nations, and are being addressed through a variety of policies in a variety of fora. Close cooperation—for example, in the summit framework, in the IMF, and in the OECD—in analyzing problems and designing domestic responses help minimize the danger of inconsistent or conflicting policies and help develop agreement on the main lines of economic strategy. Close cooperation among the major nations in the wake of the 1973–74 oil crisis helped avoid a destructive response to unprecedented balance of payments problems and movement of the world economy into recession. As we enter the 1980's, following yet another dramatic oil shock, the international community has reaffirmed the need to respond in a coordinated and cooperative way, and has reached essential agreement on the outlines of a strategy for basic structural adjustment. Recognition of the need and formulation of the strategy are essential first steps. Successful implementation will require courage and persistence throughout the oil-importing world.

But a successful adjustment is not, indeed cannot be, the sole responsibility of the oil-importing countries.

### Responsibilities of the oil-exporting nations

The oil exporters, largely the members of OPEC, have responsibilities as well. They also are important members of a highly interdependent world economic and political system whose stability must clearly be in their own interest. They must begin to act more in recognition that misuse of their enormous economic power can seriously damage the global economy and their own economies. At the same time, they must also use their large financial resources to help facilitate the required adjustments by the oil-importing world to the changed economic environment.

I believe that the OPEC countries' responsibilities to the global economy are several:

*First*, they need to follow a responsible oil-pricing policy. Uncertainty over prices and abrupt changes in them clearly have an adverse effect on inflationary expectations and investment behavior.

*Second*, the world needs to be assured of a constancy of global oil supplies. Investment strategies and macroeconomic policies aimed at reducing oil dependence and restructuring production processes can work only in an environment in which supply does not fluctuate erratically.

*Third*, there is a need for OPEC countries to follow responsible investment strategies. The world economy requires longer term investment funds to facilitate and match the needed adjustment efforts, which inevitably will take time. The OPEC nations can play an important role in assuring that the recycling process works smoothly.

*Fourth*, OPEC has a special responsibility to the developing countries. Ten years ago, the cost of oil to the LDC's was approximately 3 percent of their export receipts. It now takes about 25 percent of their exports to pay their oil bill. This drain of scarce foreign exchange resources calls for a particularly painful adjustment by the LDC's and ultimately detracts from their development efforts. Future OPEC investment strategies should include a greater portion of their funds going directly to the LDC's to finance external deficits and investment projects.

### Role of the private and the international financial institutions: A global response to recycling

A key challenge for the world economy in the 1980's will be the financing and adjustment of the large imbalances in international payments arising from the oil price increases. The institutions represented at this conference will play a critical role in determining whether we succeed in this recycling effort.

In some ways, the world payments situation today is reminiscent of the situation following the major oil price increases of 1973–74. The private financial markets, particularly the commercial banks, provided the lion's share of the financing. The

private markets will again have to perform the bulk of the recycling task: there is no realistic alternative.

But in contrast with the relatively rapid falloff in the OPEC surplus during 1976-78, it is likely that the current large world payments imbalances will persist for some time. The softening in the real price of oil that occurred in the mid-1970's cannot be counted on. Moreover, indications are that some OPEC countries will trim back their development efforts and thus that their imports will not grow at the rapid rate of earlier years. Consequently, while the OPEC surplus will probably edge down from the \$120 billion or so projected for 1980, we must expect sizable surpluses, and sizable requirements for balance of payments financing, over the next few years.

As they did in the post-war reconstruction period, the Bretton Woods institutions—the IMF and the World Bank group—are preparing to play a central role in addressing the financing and structural adjustment needs facing the world today.

The IMF is positioning itself to meet the potentially large demands for balance of payments financing that may arise, and to assist countries in undertaking programs to revitalize their economies. An increase in IMF quotas is in process, and legislation providing for U.S. participation in that general increase is now before the Congress. At the April meeting of the ministerial-level Interim Committee in Hamburg, the IMF Managing Director was encouraged to explore the possibility of borrowing additional funds directly from major surplus countries should the need arise. The Fund is moving to lengthen the period of adjustment associated with its financing, and to place greater emphasis on expanding and rationalizing the productive base in borrower countries, in recognition of the structural nature of some of the changes that must be made. The IMF is also exploring ways to strengthen its surveillance over exchange arrangements and balance of payments adjustment policies, to encourage more timely and effective action by all countries, including those countries which do not use Fund resources.

These efforts by the IMF closely parallel major initiatives being undertaken by the *multilateral development banks* (MDB's). MDB loan commitments represent by far the largest official source of external capital for the developing world, equivalent to \$14 billion in 1979. These loans contribute in a major way to economic growth and stability in the recipient countries.

In recognition of the basic change in the world economy, the World Bank is adapting its lending programs to facilitate needed adjustment. For example, the Bank, with strong U.S. support, is initiating a new program of nonproject lending for structural adjustment. Moreover, the World Bank plans to finance oil and gas projects which, combined with other official and private financing, will total more than \$33 billion over the next 5 years. Consideration is also being given to measures to expand the Bank's cofinancing arrangements with private lenders.

The ability of the IMF and the MDB's to play a strong, constructive role in dealing with present problems requires that they have adequate resources. Vital important authorization legislation is now pending in the Congress for an increase in the U.S. quota in the IMF and for the U.S. contribution to the sixth replenishment of the International Development Association. Timely congressional approval of this legislation, for the full amounts negotiated, is central to U.S. interests—political, economic and humanitarian—and to assuring a cooperative global response to the challenge of the 1980's.

## Conclusion

The problems of inflation, of energy, of international finance that we face are all too apparent.

Meeting the challenges they pose will not be easy. It will require recognition and acceptance of shared responsibilities by nations in diverse positions. Major structural change in our economies—and that is clearly what is required—is difficult and painful. It is always resisted by powerful interests, impeded by natural attachments to familiar ways and slowed by simple inertia.

So the task is great. But so too is the prize we seek—growing economies with inflation under control, with rising real incomes, with energy and financial equilibria appropriate to the new energy era in which we now live.

It is a prize that eluded us in the 1970's. Now we must summon the economic wisdom and, even more, the political will to grasp it in this new decade.

**Exhibit 68.—Text of declaration issued following the meeting of heads of state and government of Canada, the Federal Republic of Germany, France, Italy, Japan, the United Kingdom of Great Britain and Northern Ireland, and the United States of America, June 23, 1980, in Venice, Italy**

### **Introduction**

1. In this, our first meeting of the 1980's, the economic issues that have dominated our thoughts are the price and supply of energy and the implications for inflation and the level of economic activity in our own countries and for the world as a whole. Unless we can deal with the problems of energy, we cannot cope with other problems.

2. Successive large increases in the price of oil, bearing no relation to market conditions and culminating in the recent decisions by some members of the Organization of Petroleum Exporting Countries at Algiers, have produced the reality of even higher inflation and the imminent threat of severe recession and unemployment in the industrialized countries. At the same time they have undermined and in some cases virtually destroyed the prospects for growth in the developing countries. We believe that these consequences are increasingly coming to be appreciated by some of the oil exporting countries. The fact is that the industrialized countries of the free world, the oil-producing countries and the nonoil developing countries depend upon each other for the realization of their potential for economic development and prosperity. Each can overcome the obstacles to that development but only if all work together and with the interests of all in mind.

3. In this spirit we have discussed the main problems that confront us in the coming decade. We are confident in the ability of our democratic societies, based on individual freedom and social solidarity, to meet these challenges. There are no quick or easy solutions. Sustained efforts are needed to achieve a better future.

### **Inflation**

4. The reduction of inflation is our immediate top priority and will benefit all nations. Inflation retards growth and harms all sectors of our societies. Determined fiscal and monetary restraint is required to break inflationary expectations. Continuing dialogue among the social partners is also needed for this purpose. We must retain effective international coordination to carry out this policy of restraint and also to guard against the threat of growing unemployment and worldwide recession.

5. We are also committed to encouraging investment and innovation so as to increase productivity, to fostering the movement of resources from declining into expanding sectors so as to provide new job opportunities and to promoting the most effective use of resources within and among countries. This will require shifting resources from government spending to the private sector and from consumption to investment and avoiding or carefully limiting actions that shelter particular industries or sectors from the rigors of adjustment. Measures of this kind may be economically and politically difficult in the short term, but they are essential to sustained noninflationary growth and to increasing employment, which is our major goal.

6. In shaping economic policy, we need a better understanding of the long-term effects of global population growth, industrial expansion and economic development generally. A study of trends in these areas is in hand, and our representatives will keep these matters under review.

### **Energy**

7. We must break the existing link between economic growth and consumption of oil, and we mean to do so in this decade. This strategy requires conserving oil and substantially increasing production and use of alternative energy sources. To this end, maximum reliance should be placed on the price mechanism, and domestic prices for oil should take into account representative world prices. Market forces should be



supplemented where appropriate by effective fiscal incentives and administrative measures. Energy investment will contribute substantially to economic growth and employment.

8. We welcome the recent decisions of the European Community, the International Energy Agency and the Organization for Economic Cooperation and Development regarding the need for long-term structural changes to reduce oil consumption, continuing procedures to monitor progress, the possible use of oil ceilings to deal with tight market conditions and coordination of stock policies to mitigate the effect of market disruption. We note that the member countries of the I.E.A. have agreed that their energy policies should result in their collective 1985 net oil imports being substantially less than their existing 1985 group objective and that they will quantify the reduction as part of their continuing monitoring efforts. The potential for reduction has been estimated by the I.E.A. Secretariat, given existing uncertainties, at around 4 million barrels a day.

9. To conserve oil in our countries:

We are agreed that no new baseload, oil-fired generating capacity should be constructed save in exceptional circumstances, and the conversion of oil-fired capacity to other fuels should be accelerated.

We will increase efforts, including fiscal incentives where necessary, to accelerate the substitution of oil in industry.

We will encourage oil-saving investments in residential and commercial buildings, where necessary by financial incentives and by establishing insulation standards. We look to the public sector to set an example.

In transportation, our objective is the introduction of increasingly fuel-efficient vehicles. The demand of consumers and competition among manufacturers are already leading in this direction. We will accelerate this progress, where appropriate, by arrangements or standards for improved automobile fuel efficiency, by gasoline pricing and taxation decisions, by research and development and by making public transport more attractive.

10. We must rely on fuels other than oil to meet the energy needs of future economic growth. This will require early resolution and wide-ranging actions. Our potential to increase the supply and use of energy sources other than oil over the next 10 years is estimated at the equivalent of 15-20 million barrels daily of oil. We intend to make a coordinated and vigorous effort to realize this potential. To this end, we will seek a large increase in the use of coal and enhanced use of nuclear power in the medium term and a substantial increase in production of synthetic fuels, in solar energy and other sources of renewable energy over the longer term.

11. We shall encourage the exploration and development of our indigenous hydrocarbon resources in order to secure maximum production on a long-term basis.

12. Together we intend to double coal production and use by early 1990. We will encourage long-term commitments by coal producers and consumers. It will be necessary to improve infrastructures in both exporting and importing countries, as far as is economically justified, to insure the required supply and use of coal. We look forward to the recommendations of the international coal industry advisory board. They will be considered promptly. We are conscious of the environmental risks associated with increased coal production and combustion. We will do everything in our power to insure that increased use of fossil fuels, especially coal, does not damage the environment.

13. We underline the vital contribution of nuclear power to a more secure energy supply. The role of nuclear energy has to be increased if world energy needs are to be met. We shall, therefore, have to expand our nuclear generating capacity. We will continue to give the highest priority to insuring the health and safety of the public and to perfecting methods of dealing with spent fuels and disposal of nuclear waste. We reaffirm the importance of insuring the reliable supply of nuclear fuel and minimizing the risk of nuclear proliferation.

14. The studies made by the international nuclear fuel cycle evaluation group, launched at the London Summit in 1977, are a significant contribution to the use of nuclear energy. We welcome their findings with respect to increasing predictable supplies, the most effective utilization of uranium sources, including the development of advanced technologies, and the minimization of proliferation risks, including

support of International Atomic Energy Agency safeguards. We urge all countries to take these findings into account when developing policies and programs for the peaceful use of nuclear energy.

15. We will actively support the recommendations of the international energy technology group, proposed at the Tokyo summit last year, for bringing new energy technologies into commercial use at the earliest feasible time. As far as national programs are concerned, we will by mid-1981 adopt a two-phased approach: first, listing the numbers and types of commercial scale plants to be constructed in each of our countries by the mid-1980's, and, second, indicating quantitative projections for expanding production by 1990, 1995 and 2000, as a basis for future actions.

As far as international programs are concerned, we will join others in creating an international team to promote collaboration among interested nations on specific projects.

16. A high-level group of representatives of our countries and of the E.E.C. commission will review periodically the results achieved in these fields.

17. Our comprehensive energy strategy is designed to meet the requirements of the coming decade. We are convinced that it can reduce the demand for energy, particularly oil, without hampering economic growth. By carrying out this strategy we expect that, over the coming decade, the ratio between increases in collective energy consumption and economic growth of our countries will be reduced to about 0.6, that the share of oil in our total energy demand will be reduced from 53 percent now to about 40 percent by 1990 and that our collective consumption of oil in 1990 will be significantly below present levels so as to permit a balance between supply and demand at tolerable prices.

18. We continue to believe that international cooperation in energy is essential. All countries have a vital interest in a stable equilibrium between energy supply and demand. We would welcome a constructive dialogue on energy and related issues between energy producers and consumers in order to improve the coherence of their policies.

### **Relations with developing countries**

19. We are deeply concerned about the impact of the oil price increases on the developing countries that have to import oil. The increase in oil prices in the last two years has more than doubled the oil bill of these countries, which now amounts to over \$50 billion. This will drive them into ever-increasing indebtedness and put at risk the whole basis of their economic growth and social progress unless something can be done to help them.

20. We approach in a positive spirit the prospect of global negotiations in the framework of the United Nations and the formulation of a new international development strategy. In particular, our object is to cooperate with the developing countries in energy conservation and development, expansion of exports, enhancement of human skills and the tackling of underlying food and population problems.

21. A major international effort to help these countries increase their energy production is required. We believe that this view is gaining ground among oil-exporting countries. We ask the World Bank to examine the adequacy of the resources and the mechanisms now in place for the exploration, development and production of conventional and renewable energy sources in oil-importing developing countries, to consider means, including the possibility of establishing a new affiliate or facility by which it might improve and increase its lending programs for energy assistance, and to explore its findings with both oil-exporting and industrial countries.

22. We are deeply conscious that extreme poverty and chronic malnutrition afflict hundreds of millions of people of developing countries. The first requirement in these countries is to improve their ability to feed themselves and reduce their dependence on food imports. We are ready to join with them and the international agencies concerned in their comprehensive longterm strategies to increase food production and to help improve national as well as international research services. We will support and, where appropriate, supplement initiatives of the World Bank and of the Food and Agricultural Organization and to improve grain storage and food-handling facilities.

We underline the importance of wider membership of the new aid convention and of an equitable replenishment of the International Fund for Agricultural Development.

23. High priority should be given to efforts to cope with population growth and to existing United Nations and other programs for supporting these efforts.

24. We strongly support the general capital increase of the World Bank, increases in the funding of the regional development banks and the sixth replenishment of the International Development Association. We would welcome an increase in the rate of lending of these institutions within the limits of their present replenishments, as needed to fulfill the programs described above. It is essential that all members, especially the major donors, provide their full contributions on the agreed schedule.

25. We welcome the report of the Brandt commission. We shall carefully consider its recommendations.

26. The democratic industrialized countries cannot alone carry the responsibility of aid and other different contributions to developing countries; it must be equitably shared by the oil-exporting countries and the industrialized Communist countries. The personal representatives are instructed to review aid policies and procedures and other contributions to developing countries and to report back their conclusions to the next summit.

### Monetary problems

27. The situation created by large oil-generated payments imbalances, in particular those of oil-importing developing countries, requires a combination of determined actions by all countries to promote external adjustment and effective mechanisms for balance-of-payments financing. We look to the international capital market to continue to play the primary role in rechanneling the substantial oil surplus funds on the basis of sound lending standards. We support the work in progress by our monetary authorities and the Bank for International Settlements designed to improve the supervision and security of the international banking system. The private banks could usefully supplement these efforts.

28. Private lending will need to be supplemented by an expanded role for international institutions, especially the International Monetary Fund. We are committed to implementing the agreed increase in the I.M.F. quotas and to supporting appropriate borrowing by the fund, if needed to meet financing requirements of its members. We encourage the I.M.F. to seek ways in which it could, within its guidelines or conditionally, make it more attractive for countries with financing problems to use its resources. In particular, we support, the I.M.F.'s examination of possible ways to reduce charges on credits to low-income developing countries. The I.M.F. and the World Bank should work closely together in responding to these problems. We welcome the bank's innovative lending scheme for structural adjustment. We urge oil-exporting countries to increase their direct lending to countries with financial problems, thus reducing the strain on other recycling mechanisms.

29. We reaffirm our commitment to stability in the foreign exchange markets. We note that the European Monetary System has contributed to this end. We will continue close cooperation in exchange-market policies so as to avoid disorderly exchange-rate fluctuations. We will also cooperate with the I.M.F. to achieve more effective surveillance. We support continuing examinations by the I.M.F. of arrangements to provide for a more balanced evolution of the world reserve system.

### Trade

30. We are resolved further to strengthen the open world trading system. We will resist pressures for protectionist actions, which can only be self-defeating and aggravate inflation.

31. We endorse the positive conclusion of the multilateral trade negotiations and commit ourselves to early and effective implementation. We welcome the participation of some of our developing partners in the new nontariff codes and call upon others to participate. We also call for the full participation of as many countries as possible in strengthening the system of the General Agreement on Tariffs and Trade. We urge the more advanced of our developing partners gradually to open their markets over the coming decade.



32. We reaffirm our determination to avoid a harmful export-credit race. To this end we shall work with the other participants to strengthen the international arrangement on export credits with a view to reaching a mutually acceptable solution covering all aspects of the arrangement by 1 December 1980. In particular we shall seek to bring its terms closer to current market conditions and reduce distortions in export competition, recognizing the differentiated treatment of developing countries in the arrangement.

33. As a further step in strengthening the international trading system, we commit our governments to work in the United Nations toward an agreement to prohibit illicit payments to foreign government officials in international business transactions. If that effort falters, we will seek to conclude an agreement among our countries, but open to all, with the same objective.

### Conclusions

34. The economic message from this Venice summit is clear. The key success in resolving the major economic challenges which the world faces is to achieve and maintain a balance between energy supply and demand at reasonable levels and at tolerable prices. The stability of the world economy, on which the prosperity of every individual country relies, depends upon all of the countries concerned, recognizing their mutual needs and accepting their mutual responsibilities. Those among us whose countries are members of the European Community intend to make their efforts within this framework. We, who represent seven large industrialized countries of the free world, are ready to tackle our own problems with determination and to work with others to meet the challenges of the coming decade, to our own advantage and to the benefit of the whole world.

### Exhibit 69.—Press communique of the Ministerial Meeting of the Group of Ten, September 27, 1980, in Washington, D. C.

1. The Ministers and Central Bank Governors of the ten countries participating in the General Arrangements to Borrow met in Washington D.C. on September 27, 1980 under the Chairmanship of Mr. P. Hatry, Minister of Finance of Belgium. The Managing Director of the International Monetary Fund, Mr. Jacques de Larosiere, took part in the meeting, which was also attended by the President of the Swiss National Bank, Mr. F. Leutwiler, the Secretary-General of the Organization for Economic Cooperation and Development, Mr. E. van Lennep, the Economic Advisor of the Bank of International Settlements, Mr. A. Lamfalussy, and the Vice President of the Commission of the European Communities, Mr. Francois-Xavier Ortoli.

2. The Ministers and Governors noted with concern that the outlook for the world economy has not improved since their last meeting in April. The world economy continues to be faced with a high level of inflation, sluggish growth of output, an unstable energy market and large payments imbalances. They emphasized that these problems call for close cooperation between all members of the international community.

3. The Ministers and Governors continue to attach great importance to the fight against inflation and to the implementation of effective energy-saving policies, and oil-substitution programs. While the recent slowdown in major industrial countries' rates of inflation is an encouraging development, they consider that at the present time there is little scope for a relaxation of monetary, budgetary, and other policies. They also stressed the need to supplement the instruments of demand management with structural policies designed to improve supply conditions. They re-emphasized the importance of avoiding protectionist measures at a time of slow growth of world trade and widening balance of payments disequilibria.

4. The Ministers and Governors expressed particular concern about the sharp deterioration in the current-account balances of many countries. While recognizing that the international banking system and surplus countries will have to play a major role in recycling, they re-affirmed their position that it is desirable for the IMF to

assume an enlarged role in the financing and adjustment of payments imbalances. They welcome the preparatory work accomplished in this context.

5. In that connection, the Ministers and Governors recognized the need for a larger volume of lending by the Fund and for longer adjustment periods. At the same time, they stressed that the basic character of Fund lending should be preserved and that changes in the Fund lending policies that are called for in the present circumstances should be kept under review. The Ministers and Governors also emphasized the importance of a closer co-operation between the Fund and the World Bank which, however, should not alter the respective character of the two institutions.

6. As regards the financing of enlarged access to the Fund's resources, the Ministers and Governors emphasized that primary reliance should be placed on Fund quotas. At the same time they recognized that in the present situation increased recourse to borrowing is likely to prove necessary. In seeking additional resources the Fund should endeavour to find lenders and to obtain terms which take into account both the special nature of the institution and the needs of the borrowing countries.

7. The Ministers and Governors agreed that the possibility of further allocations of SDRs should be further considered.

8. Mr. A. Mac Eachen, Deputy Prime Minister and Minister of Finance of Canada, was elected Chairman of the Group of Ten for the following year.

**Exhibit 70.—Communique of the Interim Committee of the Board of Governors of the International Monetary Fund on the International Monetary System, September 29, 1980, issued after its 15th meeting in Washington, D. C.**

1. The Interim Committee of the Board of Governors of the International Monetary Fund held its fifteenth meeting in Washington, D.C. on September 28, 1980. Mr. Hannes Androsch, Vice Chancellor and Minister of Finance of Austria presided over the meeting in the absence of the Chairman of the Committee, Mr. Filippo Maria Pandolfi, Minister of the Treasury of Italy. Mr. Jacques de Larosiere, Managing Director of the International Monetary Fund, participated in the meeting. The meeting was also attended by: Mr. G. D. Arsenis, Director of Money, Finance and Development Division, UNCTAD; Mr. Alexandre Lamfalussy, Economic Adviser and Head of the Monetary and Economic Department, BIS; Mr. Emile van Lennep, Secretary-General, OECD; Mr. F. Leutwiler, President, Swiss National Bank; Mr. M. G. Mathur, Deputy Director-General, GATT; Mr. Robert S. McNamara, President, IBRD; Mr. Francois-Xavier Ortoli, Vice-President, CEC; Mr. Jean Ripert, Under-Secretary-General for International Economic and Social Affairs, UN; Mr. Cyrus Sassanpour, Head, International Money and Finance Unit, OPEC; and Mr. Cesar E. A. Virata, Chairman, Development Committee. Mr. Wang Weicai, Vice-President, Bank of China, also attended.

2. The Committee discussed the world economic outlook and the policies appropriate in the current situation. Noting that the key features of the world economic situation had not changed much since its April meeting in Hamburg, the Committee was again concerned particularly with two problems: worldwide inflation and the external payments imbalances of non-oil developing countries.

The Committee remained convinced that the top priority being given in many countries to the fight against inflation must not be relaxed. Reduction of inflation and inflationary expectations was considered necessary for the restoration of conditions for better investment performance and sustained economic growth. Although recognizing that slow growth of output is a key feature of the current situation, the Committee cautioned against any premature shift to expansionary monetary and fiscal policies. It stressed that the broad objective must be to establish the basis for sustained growth and improved employment prospects, with relative price stability over the longer run.

The Committee noted the dramatic increases in the deficits of the non-oil developing countries and expressed concern about the problems of financing such deficits, especially in the case of the low-income countries. The Committee foresaw a great and urgent need for more official development assistance to the latter countries from the industrial and oil exporting countries. This need reflects the inadequacy of

the current flow of imports to low-income countries, the erosion of their external financial positions in obtaining even this flow, their limited access to international financial markets, and their requirements for sustained rates of growth.

For developing countries, the Committee attached importance to adequate access to markets for their exports. Industrial countries were urged to avoid protectionist measures and to maintain or expand the great advantages—for themselves, as well as for many developing countries—provided by an open trading environment. Noting that many developing countries will continue to need large amounts of external credit on market terms, the Committee also urged industrial countries to avoid measures that might restrict the access of developing countries to their capital markets. It was observed that a number of developing countries themselves could contribute to maintenance or expansion of the necessary capital inflows by following policies designed to bolster confidence regarding their economic prospects.

3. The Committee discussed the developments in the Fund's policies on the use of its resources and the prospects for the Fund's liquidity.

(a) The Committee welcomed the work done by the Executive Board following the agreement reached by the Committee at its Hamburg meeting that the Fund should play a larger role in the adjustment and financing of payments imbalances in prospect for many members of the Fund. Under this policy, various aspects of which will still need to be elaborated by the Executive Board, members of the Fund making strong efforts to correct their balance of payments problems over a reasonable period through the pursuit of sound demand and supply policies would be able to obtain, on appropriate terms of conditionality, considerably larger amounts of assistance from the Fund than were available in the past. The Committee endorsed the Executive Board's conclusion that amounts up to an annual limit of 200 percent of quota (excluding uses under the Compensatory and Buffer Stock Financing Facilities) i.e., for a total of 600 percent of quota over a three-year period, would be a reasonable guideline in the present circumstances. The members of the Committee noted with satisfaction that, on the basis of this policy, the Fund has already agreed to provide large amounts of resources to several members in support of programs that envisage adjustment over longer periods than have been the normal practice hitherto.

(b) The Committee agreed that, in order for the Fund to be able to meet requests for assistance under this new policy on the use of its resources, it will be necessary that the Fund supplement its resources by further borrowing and, in this connection, it welcomed the steps already taken by the Managing Director. In view of the magnitude of the expected need, the Committee agreed that the Executive Board and the Managing Director should make, as soon as possible, the necessary arrangements to enable the Fund to borrow from various potential sources of financing, not excluding a possible recourse to the private markets if this were indispensable.

(c) While agreeing that, during the next few years, it will be necessary for the Fund to resort to further borrowing, the Committee wished to stress its view that the Fund should continue to place primary reliance on subscriptions under members' quotas as a source of financing of the Fund's operations. In this connection, the Committee expressed regret at the long delay in the implementation of the quota increases provided for in the Resolution of the Board of Governors on the Seventh General Review. The Committee, noting that 84 members having 58 percent of the total quotas have already consented to the increases in their quotas under that Resolution and that other members are expected to consent shortly, urged those members that have not yet consented to increases in their quotas, to make every effort to do so as soon as possible. Moreover, it endorsed the intention of the Executive Board to begin preparatory work on the Eighth General Review of Quotas. The Committee noted that this review will be the occasion to reflect in the quotas the developments in members' positions in the world economy, including a review of the criteria by which quotas are calculated.

(d) The Committee welcomed the agreement reached in the Executive Board on the establishment of a Subsidy Account designed to reduce the cost to low-income member countries of the use of the Fund's resources under the Supplementary Financing Facility and the intention of the Board to complete the arrangements for putting such an Account into effect. In this connection, the Committee noted the view of the Executive Board that a part of the proceeds from repayments of loans by the Trust Fund should be used to provide resources to the Subsidy Account. At the same



time, the Committee endorsed the efforts of the Managing Director to obtain voluntary contributions to the Subsidy Account, expressed its appreciation to those countries that had announced their intention to make such contributions, and urged all countries that were in a position to contribute but had not yet decided to do so to take such steps as would enable them to make an appropriate contribution to the funding of that Account.

(e) The Committee noted that, in response to a suggestion by the Food and Agriculture Organization and the World Food Council, the Executive Board had begun consideration of the question whether the Fund could extend temporary financial assistance to low-income member countries when such countries are adversely affected by a crop failure or a sharp increase in the world price of food items, especially cereals. The Committee further noted that, in the view of the Managing Director, it would be possible to establish, consistently with the Fund's authority and objectives, an arrangement for such assistance that would have only a limited effect on the liquidity of the Fund. Recognizing the seriousness of the problem faced by these member countries, the Committee urged the Executive Board to give prompt consideration to the matter.

4. The Committee had a discussion on the recommendations of the Program of Immediate Action of the Group of 24 relating to monetary issues on the basis of a report by the Executive Board, and, in this connection, noted the developments in the policies on the use of the Fund's resources described in paragraph 3(a) above. It also noted that the Executive Board had initiated an in-depth examination of the issues involved in these recommendations, such as those relating to the SDR allocations, the link between SDR allocations and development finance, and the participation of developing countries in the decision-making in the Fund.

The Committee endorsed the view that the important economic developments that have taken place should be taken into account in the consideration of further SDR allocations. In this connection, the Committee asked the Executive Board to give active consideration, in the months before the next meeting of the Committee, to the question of the appropriate level of SDR allocations. The Committee noted that due regard would need to be paid to the developments in international liquidity, payments imbalances, and the need for reserves as well as to the importance of strengthening the role of the SDR and its credibility as a reserve asset.

The Committee agreed that the Executive Board should carry out a more comprehensive study of a possible link between SDR allocations and development finance. This would need to be considered in the context of the proper role of the SDR in the system and the liquidity needs of the world.

On the subject of the participation of developing countries in the decision-making in the Fund, the Committee felt that the matter needed further consideration and noted the intention of the Executive Board to return to this important topic at an early date in connection with the Eighth Quota Review.

The Committee urged the Executive Board to pursue its consideration of the remaining issues raised by the recommendations of the Group of 24 with a view to arriving at widely acceptable solutions. The Board should report on these matters at the next meeting of the Committee.

5. The Committee welcomed the recent decisions of the Executive Board to simplify the SDR. Under these decisions, beginning on January 1, 1981, the currency basket for the valuation of the SDR will become identical with the one already applied for interest rate purposes. The SDR will, therefore, consist of five currencies, i.e., the U.S. dollar, the Deutsche mark, the French franc, the Japanese yen, and the pound sterling. In the view of the Committee, this important action, which gives practical effect to the Committee's recommendation at its meeting in Hamburg, will further enhance the attractiveness of the SDR and promote its use by private as well as public holders. The Committee also welcomed the increase in the past few months in the number of official institutions that can hold and deal in SDRs. The Committee asked the Executive Board to give early attention to the question of adjusting the SDR interest rate to the full market rate and that of eliminating the remaining reconstitution requirement.

The Committee reiterated its intention to continue the study of the subject of the Substitution Account.

6. The Committee agreed to hold its next meeting in Libreville, Gabon, on May 21, 1981.

**Exhibit 71.—Statement by Secretary Miller as Governor for the United States, October 1, 1980, at the joint annual meetings of the Boards of Governors of the International Monetary Fund and the International Bank for Reconstruction and Development and its affiliates, Washington, D.C.**

The Bretton Woods institutions continue to grow in stature and in membership. The People's Republic of China, representing nearly one-fourth of the world's population, now participates with us as a fully active partner. Our newest member, which joined yesterday, is Zimbabwe, a nation whose struggle to gain independence and freedom has engaged our high admiration and support. To all those who sit in this assembly for the first time, I offer a special welcome.

At the same time that we are welcoming new associates, we will soon be losing the services of Robert McNamara, whose vision, energy, and strength of purpose have fashioned the World Bank into a powerful and effective instrument for economic and human development. His performance, through more than a decade of wrenching change and multiplying difficulties for the developing world, has been magnificent. He deserves, and he has, the enduring gratitude of all mankind for his accomplishments. And he has our heartfelt best wishes for his future endeavors.

Bob McNamara has led the World Bank to giant accomplishments, but he is the first to point out the towering challenges ahead. He and Jacques de Larosiere have detailed for us a sobering outlook for the world's economy and people. Their perspective is not seriously contested by any of us. Together our nations face a formidable collection of problems: First and foremost, persistent inflationary pressures; weak economic growth; low productivity improvement, and capital stocks threatened with obsolescence by world energy developments; high, in many cases rising, unemployment; sharply higher oil import bills, which siphon funds from investment, development and growth to pay for essential energy imports; massive payments imbalances and financing needs.

The difficult global energy situation is a factor in all these problems. And it will not cure itself. After the oil price increases in 1973/74, the world failed to adjust sufficiently to the new situation. Instead, oil demand was temporarily reduced by a global recession. Thereafter, the oil-importing world to a large extent succeeded in financing a continuing high level of consumption, but it did not put in place the new investment needed to reduce dependence on imported oil. In many cases, the hope seemed to be that the oil and financing problems were temporary and could be resolved without fundamental changes. Indeed, there appeared to be some success, as for a brief time world inflation receded, economic activity recovered, and payments imbalances narrowed.

But a second round of massive oil price increases beginning early last year brought a renewal of the earlier difficulties. The new shock compounds the problems for a world economy already beset by strong underlying inflationary pressures and laboring under heavy external debt burdens accumulated during the 1970's.

There is no prospect of avoiding repeated oil shocks unless the oil-importing world recognizes and adjusts deliberately to a radically altered global economic and energy balance. The required adjustments involve both energy conservation and development of new energy sources. But they must also encompass measures to stimulate investment and productivity in circumstances of greatly increased energy costs. And they must be carried out in an environment of financial stability within individual national economies, to facilitate movement of resources to more productive sectors and to ensure continued flows of external financing.

We look to the oil-exporting nations to follow responsible price and production policies.

And each nation represented here must face and act upon the need for internal adjustment. Many have done so. Most have at least started the process. None, including the United States, has yet done enough to assure its satisfactory completion.

The United States is taking strong steps to reduce oil imports, to control inflation and to improve productivity.

A broad array of policies—most importantly, decontrol of domestic oil and natural gas prices—has been marshalled to encourage energy conservation and stimulate domestic energy production. Principally as a result of these efforts, U. S. oil imports are about 25 percent below the average of 1977, the peak year. This reduction is primarily the result of improved efficiency in energy use, not reduced economic activity. The amount of energy needed to produce a unit of national output has been lowered by about 10 percent since 1973.

The United States continues to pursue fiscal and monetary policies designed to limit and then reduce inflation. In addition, the President has recently proposed measures to increase the share of national output devoted to investment.

Our efforts to reduce oil imports and strengthen the U. S. economy have supported a welcome improvement in our external accounts. They have also provided a firm basis for stability and strength of the dollar on the exchange markets.

We must all recognize that our individual efforts form part of a collective international response that ultimately can succeed only if it is coordinated and cooperative. The Bretton Woods institutions originated as just such a cooperative effort. Their task was to guide the world economy from the devastation of World War II, and their success was remarkable. In subsequent decades they have adapted flexibly and imaginatively to changing needs and circumstances. But a major test lies ahead. As we enter a new decade, we must again call upon these institutions for guidance through a difficult and dangerous period.

A world accustomed to strong growth and rising living standards now faces the prospect of a decade in which performance may fall short of expectations and aspirations. Large persistent imbalances in international payments are likely. And the associated financing requirements are huge. In 1980 alone, the aggregate of current account deficits that need to be financed could reach \$150 billion.

In light of these prospects the Fund and Bank face a complementary task: the Fund to assure a judicious blend of financing and adjustment; and the Bank to assist in restructuring economies to permit development to continue as rapidly as possible.

Let me outline the U.S. view of the roles of each of these institutions.

### **The International Monetary Fund**

Looking ahead, the Fund faces truly awesome tasks. It must oversee the operation of the international monetary system at a time when pressures on that system are severe. It must encourage each member toward policies for orderly growth and price stability, in a period when the attainment of those goals is more difficult than ever before. It must see that nations follow exchange rate policies compatible with their international obligations, under conditions of enormous global payments imbalances and great uncertainty.

No one expects the Fund to fulfill these responsibilities to perfection. Our knowledge and foresight are imperfect. The Fund's authority over sovereign members is circumscribed. Its tools are limited.

But we must make sure that the Fund—the international community operating collectively—is in a position to make a maximum effort. Its approach must be right, its advice sound, its resources adequate. And we must keep in mind the longer term objective of international cooperation: in designing our approach to immediate and pressing problems, we must not lose sight of the broad goals we have set for the evolution of the international monetary system.

Let me state my message plainly: The Fund's main job will be to encourage the appropriate blend of adjustment and financing by member nations; to facilitate forms of adjustment and financing that are most supportive of a strong world economy; and to continue progress toward the kind of international monetary system we need for a secure and prosperous future.

That means improving the Fund's ability to provide financing to those countries undertaking difficult adjustment efforts. It means a greater role for the SDR and progress toward an SDR-centered international monetary system. And it means improving IMF surveillance over members' policies.



In the past several months, discussion has focused on the role of the Fund in meeting prospective financing needs and in supporting the efforts of individual nations to come to grips with adjustment problems. In Hamburg last spring, the Interim Committee endorsed in broad terms the view that the Fund should be prepared to play a much larger role in adjustment and financing. The Executive Board has worked hard to define that role in the design of adjustment programs and the expansion of members' access to Fund resources. Clearly, present circumstances call for adjustment programs with a longer term orientation than in the past. Larger amounts of Fund resources will need to be committed to countries adopting such programs over a longer period of time. The United States strongly endorses the results of the Board's work and urges its early implementation.

The Fund is presently in a satisfactory position to meet expanded calls on its resources. I am particularly pleased that the Congress has just completed final action on authorizing U. S. participation in the seventh quota increase. We will work with the Congress to complete the appropriation process, so that the general quota increase—which totals about \$25 billion—can take effect at a very early date. This will be a welcome and needed addition to the Fund's resources.

We are all agreed that quotas must remain the basic source of IMF financing. But potential demands on the IMF are substantial. As a precaution, the Managing Director has already begun to explore the possibility of IMF borrowing from surplus countries to supplement the Fund's resources in case of need.

We should also consider other prospects. The time has come for a careful examination by the Fund of the possibility of borrowing from private sources. A number of technical and legal questions must be reviewed, and there are factors that may limit the IMF's recourse to the private markets, at least over the short run. But Fund borrowing from the capital markets on a moderate scale may prove to be desirable, and I urge that the necessary preparatory work be initiated promptly.

IMF borrowing from the private markets would be fully in line with the effort to enhance the role of the SDR in the international monetary system. We welcome the recent decision by the Executive Board to adopt a five-currency basket as the uniform basis for both valuation of the SDR and calculation of the SDR interest rate. This will provide an SDR that is more compact and understandable, easier to trade and work with in foreign exchange and capital markets, but still a reserve asset that is internationally backed and representative of a large segment of the world economy.

We should go farther, and consider other steps to promote the role of the SDR in the system.

The Executive Board has been examining the question of SDR allocations for next year and the fourth basic period, beginning in 1982. Clearly, there have been major developments in the world economy since the decision was taken in 1978 on allocations for the 3 years ending in 1981. But in my view, the most effective approach to expanding the SDR's role is a relatively steady expansion of allocations, from basic period to basic period as the world economy grows. We are not persuaded that an effort to "fine tune" a single year's allocation would be appropriate or consistent with our view of the longer term evolution of the SDR's role. It is of paramount importance that we develop the credibility and reliability of the SDR as a reserve asset. We should not give the impression of tinkering with it. We will look toward a careful analysis by the Managing Director and the Executive Board of the question of allocations in the next basic period, and will consider positively a proposal by the Managing Director next spring.

The yield on the SDR has an important bearing on attitudes toward acceptance of the asset and decisions on allocations. The rate of interest on the SDR has been increased by a substantial amount over the years. I believe that it would be useful to raise further the rate of interest on the SDR, to the full market level, in order to enhance the attractiveness and therefore the usability of the asset. At the same time, we should raise the rate of remuneration to 80 percent of the full market SDR rate and eliminate the remaining residual SDR "reconstitution" obligation. Market-oriented characteristics and elimination of encumbrances can only enhance the usability and attractiveness of the SDR.

The prospect of IMF borrowing from the private markets raises in concrete terms the possibility of greater private use of SDR-denominated assets. From a longer term

perspective, we urge the Executive Board to initiate a study of other measures that might be taken to expand the use of SDR-denominated instruments by the private sector. As the private market in SDR's develops and takes hold, we propose that the World Bank give consideration to borrowing in the form of SDR-denominated securities and lending correspondingly in SDR terms, both as a means of giving further impetus to the instrument and as a technique of moderating exchange risk for the Bank's borrowers.

As another step toward expanding the role of the SDR, we urge the Executive Board to continue its work on the concept of a substitution account, which I believe would be better named a "monetary reserve account." We should not be surprised that the development of this idea takes considerable time. The SDR itself took years to define and introduce.

The steps I have mentioned today can, together make a useful contribution to strengthening the SDR and promoting its use as a respected and effective international monetary instrument. The United States has also given attention to the renewed suggestions that a link be established between the creation of special drawing rights and the provision of development assistance—a so-called SDR-aid link. Our view remains that the establishment of the proposed link would be harmful to what we regard as the fundamental objective: to develop the SDR's role as an important monetary instrument and promote orderly evolution of the international monetary system.

As the Fund carries out its expanded responsibilities in the current situation, we believe it important that it give renewed attention to strengthening its role in surveillance over the international monetary system and the policies of member countries. The United States has suggested a number of steps that could be taken toward this end. For example:

- It seems to us natural that, in seeking to promote greater symmetry of adjustment responsibilities, the Fund should seek adjustment policy statements and analyses from any country experiencing large imbalance, whether surplus or deficit.
- We have suggested that the policies and performance of individual countries be assessed against a broadly agreed global economic framework.
- We believe the Managing Director should be invited to take the initiative in consulting members where he has concerns about the appropriateness of their policies.

The Executive Board has made some progress in developing its surveillance procedures over the past year. But that progress has been disappointingly modest. We all seem to agree that effective surveillance is the essence of a smoothly functioning international monetary system. Yet, I have noticed that many who are critical of the system are the most resistant to the development of surveillance which is at the heart of its effectiveness.

The world faces extraordinary economic and financial problems and challenges. The Fund is at the center of our response. Its ability is proven. Its resources are expanding. Its policies are being adapted to changing needs. Its objectives and purposes have been endorsed by every country represented here. We have endorsed a global strategy based on the IMF's financing and adjustment policies. Now we must make it work. I urge all member nations to help the Fund give substance to its agreed role in overseeing the operations of a sound international monetary system.

## The World Bank

The welfare of the developing countries and the immense problems which they confront are of paramount concern to the United States. We recognize fully the urgency of today's development needs. The commission chaired by Chancellor Brandt has properly stressed the common interest of both industrialized and developing nations in meeting global economic problems, including the need for equitable growth in developing countries. Progress in the developing nations is essential to the health of the global economy as a whole.

It is for these reasons that the United States is so strongly committed to the work of the World Bank. Over the past 35 years, the Bank has made great strides as a project financier, financial catalyst, and institution builder. The Bank has pioneered efforts to speed human capital formation and has been in the forefront of efforts directly to reduce poverty. Bank operations have contributed enormously to development, and the Bank is now clearly established as the leader of the international community's efforts to address development concerns.

The record for developing countries since the Bank was established shows clear progress. Quality of life standards have shown significant improvement. Average per capita income has approximately doubled in real terms since 1960. Yet formidable development challenges remain.

Absolute poverty is pervasive. Serious, widespread deficiencies remain in health and nutrition, literacy and education, life expectancy, and in the overall physical and social environment. Population growth continues to add to the already immense problems of unemployment and underemployment. Rural to urban migration has fueled a rapid increase in the numbers of urban poor. In addition, there is the continuing critical need of low-income countries—with large numbers of rural poor and heavy reliance on agriculture—to improve the productivity of the small farmer.

These serious development problems have been compounded by world economic conditions. Surging oil prices, worldwide inflation, slower growth in the industrial countries, and constraints on access to external capital have combined to cast a long shadow over development prospects for the 1980's.

In the difficult decade ahead, it is of vital importance that the Bank remain at the forefront of global efforts to deal imaginatively with the changed economic situation. For its part, the United States will continue to support and encourage those adaptations in the Bank lending which effectively meet the evolving needs of the developing countries and strengthen their capacity for further growth and development. We attach great importance to the Bank's existing plans to lend approximately \$14 billion for energy development projects in oil-importing developing countries through 1985. We strongly support the Bank's search for additional ways to further expand energy development in its borrowing countries, including the possibility of an energy facility or affiliate which would consolidate and enhance the Bank's activities in this field.

The United States strongly applauds the Bank's new program to support "structural adjustment." It is a necessary response to altered global economic conditions and a radically changed world energy balance. The bank's structural adjustment loans, coordinated closely with the IMF, will serve as a catalyst for growth and help strengthen the recycling process. It is particularly appropriate for the World Bank to undertake this critical program because of its sound reputation, expertise, and long experience with the sectoral issues that are fundamental to any restructuring.

We appreciate the 1980 World Development Report's analysis of the relationship between population and other aspects of human resource development and economic growth. We look forward to increased Bank lending in the population area in coming years.

The Bank's record of solid achievement in maximizing project benefits for the poor should be maintained and the share of its lending allocated to the poorer borrowing countries should be increased. This is vitally important given the unacceptably high level of absolute poverty and the value—so impressively highlighted in the 1980 World Development Report—of human development as a tool of growth.

### **Bank financing**

The United States and other Bank members have a vital interest in encouraging effective responses by the Bank to critical world needs. It is thus of great common concern to note that the needs of the developing countries are—for the reasons highlighted in Bob McNamara's address—growing more rapidly than anticipated. Fortunately, we have already negotiated both a general capital increase (GCI) for the World Bank and a Sixth Replenishment of IDA's resources.

The United States fully supports both the GCI and IDA VI. We hope to have legislative approval for U.S. participation in IDA VI before the end of this session of



Congress. U.S. participation in the GCI will be the principal element of next year's funding request to Congress.

The agreed general capital increase of \$40 billion—increasing World Bank capital from \$45 billion—and the \$12 billion IDA VI replenishment should meet developing country needs for Bank financing over the next few years. We therefore will have time to assess carefully how best to finance the needs of the developing countries beyond these replenishments.

The United States is prepared to join other members to look at alternative ways to help support bank operations. Any reassessment of Bank financing must, of course, be done thoughtfully and deliberately, with due regard for the needs of developing countries, the need to maintain the high quality of lending standards, and the impact of future financing on the capital structure of the Bank.

We are also willing to join with others in a serious effort to improve the efficiency and effectiveness of both bilateral and multilateral concessional assistance, including channelling an increasing share to the poorest developing countries. We will also work to find practical ways ourselves to increase both the quality and quantity of such assistance.

### **Bank/Fund collaboration**

There is one additional area where I think there is a need for innovation: that is in the collaboration between the Fund and the World Bank.

When we established these twin institutions in 1946, the world was different, and the functions of the Fund and Bank were clearly separated and defined. Now the problems of short-term adjustment and the problems of development have become more intertwined, and the activities of the Fund and the Bank are focusing more on common problems.

Both developing and industrial countries have learned that an effective program of adjustment to achieve the multiple and sometimes conflicting objectives of economic policy requires attention to both demand management and the supply side of the equation. Over the years since Bretton Woods, the Fund has worked with its members in the design of demand management policies to achieve economic stabilization. The Bank has focused on the supply side in its effort to promote growth through development of sound investment strategies. In the years ahead, it is essential that the unique capabilities of these two institutions be brought to bear in a complementary and positive manner to assist countries in their adjustment efforts. The Bank and Fund should be prepared to collaborate with one another to assist member countries in assessing their economic prospects, developing effective economic programs and providing appropriate financing.

At the same time, it is also essential that the Fund and the Bank remain as autonomous institutions with distinct functions and purposes.

I know that the staffs of these two institutions have made significant strides in collaborating on adjustment programs in specific countries. At this stage, I think it would be useful to review what has been accomplished, with a view to improving the form and substance of this collaboration in the future. This review might best be undertaken under the auspices of a joint committee of the Executive Boards, supported by the staffs of both institutions.

Effective collaboration between these two institutions will help ensure their continued responsiveness to the changing needs of the world economy. We also urge consideration of steps to assure proper coordination of the borrowing policies of the two institutions. The prospect that both could be borrowing in world capital markets in the same time frame suggests the need for specific steps to assure a smooth coordination of those activities.

### **Conclusion**

The record clearly shows that the Fund and the Bank have demonstrated repeatedly their capacity to evolve, adapt and respond flexibly during periods of major economic and financial strain. The institutions work efficiently and well. They deal in realities, and give practical content to the high objectives set forth in their Articles. But their ability to continue to perform their indispensable tasks depends on the commitment of

their members to maintaining their integrity and competence and to avoiding injection of political issues into their work.

Difficult problems and challenges confront us. The Bretton Woods institutions are the central focus of our collective effort to meet those challenges successfully and cooperatively. The United States pledges its vigorous support to the Fund and Bank as they address the tasks before them. With the support of other nations represented here today, I am confident that lasting success will be achieved.

### **Developing Nations**

#### **Exhibit 72.—Text of announcement made by the Department of the Treasury, November 14, 1979, concerning the blocking of official Iranian assets**

The President today has issued an order blocking all official Iranian assets in the United States, including deposits in U.S. banks, their foreign branches, and subsidiaries in response to reported instructions that the Government of Iran is about to withdraw its funds. The purpose of this order is to insure that claims of the United States and its citizens on Iran are provided for in an orderly manner. The order does not affect accounts of persons other than the Government of Iran, the Central Bank of Iran, and other controlled entities. The precise amounts involved cannot be ascertained at this time, but there is no reason for disturbance in the foreign exchange or other markets. The President is taking this action pursuant to the International Emergency Economic Powers Act which grants the President authority "to deal with any unusual and extraordinary threat to the national security, foreign policy, or economy of the United States."

#### **Exhibit 73.—Remarks by Assistant Secretary Bergsten, January 29, 1980, before the Center for Inter-American Relations, New York, N.Y., entitled "North-South Relations: A Candid Appraisal"**

Economic and political relations between the industrialized North and the developing South have improved dramatically since the early 1970's. Six years ago, both the tone and substance of North-South relations were characterized by confrontation and hostility. A number of developing nations sought to force a radical restructuring of the world economic system. They proposed to jettison existing international economic institutions and impose a series of unilateral rights of the developing nations as the sole criterion for a "new international economic order" (NIEO).

Most industrialized nations, particularly the United States, found both the manner and the substance of these demands offensive and economically unacceptable. Some sincerely believed that the new demands of the developing countries were not in the interest of the developing countries themselves. Some resisted change simply because they found the status quo to be quite comfortable. Some believed that reform was possible, and perhaps necessary, but rightly believed that it could not come about through open confrontation and shrill rhetoric.

Fortunately, moderate voices and a willingness to consider the realistic needs of North and South alike emerged over time in both the North and South. After considerable effort and negotiations in a variety of international forums, there has occurred a great deal of international economic reform—to the substantial benefit of both North and South. To be sure, problems remain in North-South relations. But the record of the recent past demonstrates clearly that North and South can work together successfully to resolve common problems, and assure that an evolving international economic system provides mutual benefits for all nations.

I want to analyze today in some detail this rather dramatic change in international affairs, and then suggest that the most urgent task for North-South relations now is to build on that record of progress and to avoid any relapse to the sterile stand-off of just a few years ago.

### **The early 1970's: confrontation**

The confrontation of the early 1970's derived from strong differences in perceptions of the benefits flowing from the international economic system, as well as sharply divergent international economic goals. Shrill demands for a new international economic order to transfer resources unilaterally to the developing nations were made by many developing countries. These nations, largely using the highly politicized forums provided by the United Nations, harangued the North for economic imperialism and exploitation. They pushed through controversial resolutions—such as the NIEO and the Charter for Economic Rights and Duties of States—which were unacceptable to the United States and other industrialized countries.

Developing-country tactics were matched by rigid resistance on the part of the United States and some other industrialized nations. They adopted the view that few, if any, changes in the international economic system were needed. Rhetoric was high on both sides. There was little interest in negotiating meaningfully to find common ground.

Feeling both defensive and aggravated, the United States in particular was unwilling to even talk about a number of issues which seemed of critical importance to developing countries. This list included problems involving individual commodities, the establishment of a common fund, monetary matters, and problems surrounding international investment and multinational corporations. The United States put a flat ceiling on the lending program of the World Bank. U.S. concessional aid flows fell to their lowest point since World War II.

The developing nations therefore reasoned, understandably to some extent, that cooperation with the industrialized countries—particularly with the leading industrialized country, the United States—was unlikely to produce achievement of some of their most fundamental goals. The negotiating option simply wouldn't work, as they saw it. Rhetoric and intransigence precluded it as a viable option. Hence, confrontation was the only available vehicle to pursue their national goals.

The dramatic emergence of OPEC as a world power was also a heady experience for the developing nations. Many of them viewed OPEC's success as a model to emulate in their relations with the North, as well as a source of direct support for their own economic and political goals. A number of developing countries sought to form cartels for such commodities as bauxite, coffee, and copper. The developed nations heard the South's rhetoric and feared concerted Third World action. This fear, coupled with the South's sense of triumph, heightened the mood of confrontation and made each side stand firmer in its respective position.

### **The late 1970's: cooperation**

Fortunately, overall North-South relations have changed considerably since those traumatic days. There has been significant improvement in both substance and tone as positions were moderated on both sides—an improvement from which all countries can derive great satisfaction.

Former Secretary of State Kissinger's speech in September 1975 before the seventh special session of the U.N. General Assembly was the first sign that U.S. policy toward the developing nations was changing. In that speech, the United States called for an end to confrontation between developed and developing countries and for a new mode of international cooperation to ensure basic economic security for all nations. To this end, it proposed a number of new initiatives. Among them were proposals to stabilize countries' export earnings, a point of particular importance to LDC's; to assist LDC's in gaining access to long-term capital markets; to facilitate exchange of technological information; and to develop additional energy resources.

This new U.S. approach began to defuse the confrontational rhetoric and set the tone for serious negotiations on substantive issues. The United States joined the international tin and coffee agreements in 1976. The United States was instrumental in securing substantial liberalization of the compensatory financing facility (CFF) of the International Monetary Fund, which met one of the major needs of the developing countries—a balance of payments financing mechanism to help see them through periods of temporary shortfalls in export earnings. The result was immediate: drawings by developing countries alone during the world economic downturn in 1976-77



increased to \$1.9 billion, more than the \$1.2 billion drawn by the IMF membership as a whole during the entire preceding 13 years of the facility.

The agreement of industrialized, developing, and oil-producing nations to discuss a wide range of economic issues through the Conference on International Economic Cooperation (CIEC) beginning in 1975 revealed this new emphasis on cooperation in resolving common problems. In hindsight, we can see that the CIEC tried to focus on too many issues in disparate fields and to do so through political negotiations removed from the functionally specific international forums where successful results are much more likely. CIEC was, however, an important learning experience for North and South alike.

### **The objectives of U.S. policy**

Coming into office during the final phase of the CIEC experience, the Carter administration was determined to achieve widespread progress in North-South relations. It concluded, however, that comprehensive global negotiations would not promote this objective. Substantive progress could only come from diligent efforts in each of the key functional areas, based on an appreciation of the potential joint gains for both North and South from such efforts.

The new U.S. policy toward the developing countries was based upon three considerations:

- (1) The growing importance of the developing countries to U.S. security and foreign policy interests;
- (2) The importance of the developing countries to U.S. economic interests; and
- (3) The potential for mutual gains through a cooperative North-South approach in specific policy areas.

The developing countries have assumed an increasingly important role in world affairs. A number of global problems of great importance to the United States can be resolved only with the cooperation of the developing countries. The Soviet invasion of Afghanistan and the taking of U.S. hostages in Iran are clear cases in point, where LDC support—whether through votes on key resolutions in the United Nations, or in cooperation with direct U.S. responses, or in other ways—is vital to fundamental U.S. security and political interests. It is a simple truism to recognize that the prospects for LDC support on such issues of primary importance to the United States will be enhanced by U.S. cooperation on issues of keen interest to them.

In a similar manner, U.S. economic interests require effective relations with the developing countries. The United States sells more than 20 percent of its exports to nonoil developing countries, equivalent to \$34 billion in 1978. Twenty-five percent of U.S. manufactured exports went to nonoil developing countries in 1978, more than to the entire European community. More than half a million U.S. manufacturing jobs produce for export to nonoil LDC's. The United States is highly dependent upon the developing countries for supplies of crucial raw materials and a number of tropical agricultural products.

This increasing economic interdependence offers considerable potential for joint gains in a number of areas. Energy price and availability, for example, have been a crucial problem for all oil-importing countries—industrialized and developing. Trade offers potential for growing markets and increased specialization for North and South alike with a resulting increase in global efficiency, stimulus to economic growth and employment, and lower consumer costs. Greater commodity price stability benefits both producers and consumers. Development assistance can provide the needed stimulus for economic growth which will eventually enable the LDC's to attract private capital and begin importing foreign manufactured goods, as well as manifesting our humanitarian desires to better the lives of people everywhere.

### **The recent record**

The United States, particularly since 1977, has therefore adopted a positive and comprehensive approach to North-South economic relations. This change in U.S. attitudes has made possible common action by the industrialized nations as a group.

This in turn has revived the prospects for the cooperative approach to North-South relations, and made possible the improvement of recent years.

Progress has been made on a number of fronts. In the last 2 years, new multilateral initiatives undertaken by the industrialized countries acting together will make almost \$100 billion in additional funds available to the developing countries. Some of these funds are in the form of concessional assistance. Some represent intermediation in the private capital markets. Some offer short-term balance of payments support, as part of efforts to improve the functioning of the international monetary system for the benefit of all countries. All provide real economic assistance to those nations. In addition, we have negotiated a series of nonquantifiable breakthroughs in such areas as trade and commodity policy. These achievements are all the more impressive in light of the economic difficulties which have beset both the United States and most other national economies during this period. Let me enumerate.

*Multilateral development banks (MDB's).*—The United States has supported a capital increase for the World Bank of \$40 billion. We took the lead in negotiating a replenishment of almost \$10 billion for the Inter-American Development Bank. We participated in negotiating a new replenishment of over \$2 billion for the Asian Development Fund, and have agreed to U.S. membership in the African Development Bank and an increase in AFDB capital of \$4.5 billion. For IDA, the soft loan window of the World Bank which is the most important concessional assistance institution in the world, we contributed 31 percent to the fifth replenishment of \$7.6 billion in 1977 and have just pledged 27 percent to the sixth replenishment of \$12 billion. To fulfill these pledges, the administration worked with Congress to obtain a record level of appropriations of \$2.5 billion for fiscal year 1979 for the MDB's, up from only \$700 million voted for fiscal year 1977 before this administration took office.

*Strengthened monetary system.*—The United States has supported a number of steps to strengthen the international monetary system and the International Monetary Fund (IMF), the central institution of the system. These steps are beneficial to all countries, developed and developing alike, for they ensure a strong financial structure to facilitate the expansion and balanced growth of the world economy.

As the world's central monetary institution, the IMF provides the basic framework for international monetary cooperation and makes financial resources available to all member countries in times of balance of payments need. The United States has supported a series of recent actions to strengthen the financial capabilities of the IMF to meet the demands on its resources in a period of rapid change and political strain.

The Supplementary Financing Facility, with resources amounting to about \$10 billion, was established last year to supplement temporarily regular IMF assistance to countries with particularly severe payments problems; since its commencement last spring, arrangements for \$1.8 billion have been agreed under the facility—all for the benefit of developing countries.

An increase in members' quotas was implemented in early 1978, to further enhance the IMF's permanent resources, and an additional 50-percent increase in quotas is scheduled to take effect later this year—which, taken together, will increase LDC quotas by about \$8.4 billion.

SDR allocations have been resumed, to help meet rising needs for world liquidity and promote the role of the SDR as the principal reserve asset in the monetary system. Over the period 1979–81, nonoil developing countries will receive allocations of about \$3.6 billion.

The IMF's compensatory financing facility has been further liberalized to provide temporary financing to countries experiencing a shortfall in export earnings caused by circumstances beyond their control. The fund has lengthened the repayment period under its Extended Fund Facility to provide countries with more time in which to undertake major structural changes in their economies. And it is considering the possibility of lowering interest costs of the Supplementary Financing Facility.

*Trade.*—The United States reinvigorated the deadlocked multilateral trade negotiations (MTN) and brought them to a successful conclusion. The resulting agreements provide a 25-percent cut in developed country tariffs applicable to LDC exports. U.S. tariff cuts on LDC products, excluding textiles and apparel, average about 35 percent.

New nontariff codes on subsidies, government procurement, standards, import licensing, and customs valuation will provide a much more open and stable environment for future trade growth. The agreements also provide a permanent legal basis for special and more favorable treatment of developing countries, accompanied by more liberal rules on trade measures taken for development purposes. Since opportunities for trade expansion are probably the single most important feature of the world economy for most developing nations, the MTN agreements mark an enormous step forward in North-South economic relations.

As probably the most important area of U.S. economic interaction with developing countries, trade provides the clearest example of mutual benefits for industrialized and developing countries alike. The nonoil LDC's are by far the fastest growing market for U.S. exports, where our sales have more than doubled from \$16 billion in 1973 to over \$34 billion in 1978.

At the same time, U.S. imports from developing countries grew from nearly \$16 billion to \$40 billion over this period. Despite the fact that the United States accounts for only about 40 percent of the combined GNP of the industrial countries, in 1978 the United States took more than 52 percent of developing country manufactured exports to all industrial countries. Nearly 22 percent of all our manufactured imports in 1978 came from developing countries; the corresponding figure for all other industrial countries was less than 5 percent. U.S. economic growth since the global recession of 1975 has been particularly beneficial to the non-oil LDC's, whose exports grew much faster to the U.S. market than to either Japan or the European community.

*Energy.*—With strong support from the United States, the World Bank plans to support oil and gas projects totaling \$7.7 billion over the next 5 years—which should produce an additional 2 million barrels of oil equivalent a day. Our own Overseas Private Investment Corporation (OPIC) has established political risk insurance for oil exploration, production, and development in developing countries, with significant results already. These multilateral and bilateral efforts will help reduce the dependence of developing countries on expensive oil imports and, at the same time, improve the world energy balance.

*Commodities.*—The United States supports the negotiation of stabilization agreements to dampen commodity price fluctuations, which can accelerate inflation for consuming countries and disrupt investment and production in producing countries. An international sugar agreement was finalized in September 1977. The framework of an agreement for the common fund was agreed in March 1979. A rubber agreement was completed in October 1979. The United States, as a result of congressional action last month, will now contribute its share to the buffer stock of the tin agreement.

*Development aid.*—We and other donors have substantially increased concessional assistance to the poorer developing countries. Between 1970 and 1978, aid receipts by countries with per capita incomes below \$400 have tripled. Measured in relation to the GNP of the recipient countries—which is probably the best overall indicator of the contribution of aid flows to a recipient's development—total official aid to the poor countries has sharply increased over the past few years. For the least developed countries, aid receipts increased from 2.6 percent of the recipients' combined GNP in 1969–71 to 10.3 percent in 1978. For all countries with per capita GNP below \$400, the growth was from 3.3 to 4.7 percent.

*Food.*—The Carter administration joined in supporting the creation of a \$1 billion International Fund for Agricultural Development (IFAD). U.S. farmers, acting on Government incentives, placed 35 million tons of grain in reserve during 1977–78; the value of this reserve was demonstrated last year when 14 million tons were released into the market in response to rising world demand. By ending the setaside program in agriculture, we have helped provide more food for the world. We have proposed the creation of a special food aid reserve of 4 million tons of grain. We have pledged 4.5 million tons of food aid annually under the Food Aid Convention, nearly half of its 10 million ton target. The United States has been in the forefront in urging the multilateral development banks to help develop effective food strategies; one-third of IBRD/IDA loans in 1980 will support LDC agricultural sectors, including rural development.

*Science and technology.*—The administration has proposed the establishment of an Institute for Scientific and Technological Cooperation (ISTC) to strengthen develop-



ing country capacity to conduct scientific and technological research on key development problems.

### The responsibilities of the South

All these developments provide concrete evidence of the willingness of the United States and the other industrialized countries to cooperate fully and effectively in responding to the needs of the developing countries. The record clearly belies any view that the United States has been ungenerous in its help, or protectionist in its trade, or unresponsive to the needs of others.

As already indicated, we have taken these steps because we believe both in responding to the needs of others and in the prospects for mutual gains from properly conceived North-South relations. From our views concerning mutual gains, it follows naturally that we believe in mutual responsibility for the successful operation of the international economic system. It is in our interest, as well as that of the developing countries, that they assume a greater role in the management of the global economy.

For example, a number of LDC's contributed substantially to the successful outcome of the MTN by liberalizing their own import regimes and agreeing to phase out their export subsidies. Several have become modest aid donors, and now contribute to the same international lending agencies from which they borrowed only a few years ago. We expect that key developing countries will continue to make positive contributions in other international economic negotiations in the months and years ahead.

Latin America provides some of the best examples of the successful policy of mutual gains and shared responsibility. The majority of these countries—which are in the forefront of economic progress in the developing world—are no longer dependent on concessional aid. Some of these Latin American countries have begun to mount their own foreign assistance efforts to help the poorer nations in their midst.

To be sure, pockets of poverty and other severe development problems still exist in Latin America. But many of these countries are in the process of graduating from a position of dependency to full-fledged membership in the international economic system, making full use of private capital markets to finance their economic development and taking extensive advantage of world trading opportunities. The pace of such graduation has been slowed by the devastating impact of soaring oil prices, rampant inflation, and world economic slowdown. But its eventual culmination seems assured, and we welcome their rapid movement toward full participation in the world economy.

### Lessons for the future

The primary lesson to be drawn from the progress achieved over the past 5 years is that the cooperative approach can work. With good will and hard work on both sides, mutual benefits can be derived from serious and flexible negotiation on specific issues of concern to all nations. The international economic order can be reformed in an evolutionary way to further the interests of all countries. Confrontation can be avoided.

But we must be alert to the risks of retrogression. We still occasionally hear harsh rhetoric concerning North-South relations, and calls for unrealistic concessions, reminiscent of an uglier period of 6 or 7 years ago. Some cynics say that such rhetoric is harmless. Unfortunately, it isn't. Such rhetoric is heard by North and South alike. It raises developing countries' expectations, and thus their risk of disillusionment. The American people hear it, and conclude that developing countries are ungrateful for our assistance and insensitive to our own problems—thereby jeopardizing the prospects for sustaining our policy approach of the past few years.

Such rhetoric makes it difficult to work together toward common goals. Yet we know from recent history that a return to confrontation in North-South relations would not produce further progress. To the contrary, those relations would retrogress as a result.

Indeed, if the developing countries were to press for linkages between various negotiations, as some of their present rhetoric suggests, some would have us respond by withholding positive measures unless we are given something specific in return. We

in the administration believe that this would be a bad approach, but we cannot ignore the pressures to pursue it which can result from irresponsible rhetoric from either North or South.

Unfortunately, it is not only rhetoric, linkage and incessant calls for the creation of new funds which would raise anew the specter of confrontation. Several developing countries seem again bent on seeking to control world markets for their commodity exports rather than working with consumers—within the framework of existing commodity agreements—to stabilize prices for the benefit of both. It is obviously imperative to avoid any such confrontation scenario, with industrialized and developing nations continuing to work pragmatically together to negotiate specific issues in their specific functional forums.

We have just begun, in the U.N. Committee of the Whole, to work out the substance and structure for a new round of economic negotiations. As we proceed in this endeavor, we should be careful to bear in mind the lessons of the past—that these negotiations have no chance of being fruitful unless they are undertaken in their proper functional forums with due regard for the national needs of both industrialized and developing countries. Politicizing the issues, and seeking simultaneous solutions to a multitude of problems, will only result in stalemate. As President Carter said in Caracas, in February 1978, “Real progress will come through specific, cooperative actions designed to meet specific needs—not through symbolic statements made by developing countries to recall past injustices. We need to share a responsibility for solving problems and not to divide the blame for ignoring problems.”

Another important lesson we have learned since 1973 is that the oil-importing developing countries can hardly count on OPEC to champion their interests. Developing countries have in fact been ravaged by OPEC's actions. Many development plans have been severely constrained, or completely derailed, by the high cost of oil imports as well as by the indirect impact on developed countries caused by OPEC's actions.

In 1974 it took nearly 4 percent of LDC exports to pay for their oil imports. In 1980, we estimate that it will take 25 percent. Next year alone, the increase in the import bills of oil-importing LDC's due to higher energy prices will be \$15 billion. Nonoil LDC's increasingly recognize that OPEC nations must contribute to resolving the common problems which their actions have helped to create.

## Conclusion

There has been considerable progress during the past few years in North-South relations. In the process of attaining this progress, we have sought to ensure that all of the policies we have adopted will provide benefits for the United States as well as for the developing countries. Indeed, this is the only politically viable way in which such progress can be made.

The primary task before us now is to consolidate and make full use of those international economic instruments which have recently been put in place, most of which I have discussed today. We can determine what further steps need to be taken only when we have implemented the new agreements and given them a chance to work.

At home, this requires rapid and faithful implementation—including by the Congress—of the various steps which have been worked out internationally. Abroad, it requires patience and perseverance in effectively utilizing the agreements of the late 1970's. By building on the progress made on specific issues in functionally specific forums over the past few years, we can hope to evolve a more stable and equitable world economy in the 1980's and beyond.

**Exhibit 74.—Remarks by Assistant Secretary Bergsten, February 25, 1980, before the Brazil-U.S. Business Council, Washington, D.C., entitled “The United States and Brazil: A Framework for Future Economic Relations”**

It is a pleasure to address this distinguished group of representatives to the fourth plenary meeting of the Brazil-U.S. Business Council. Although the Council has been in

existence for only 3 1/2 years, it has come to play an important role in strengthening cooperation on economic issues affecting Brazil and the United States and in fostering a closer understanding between our two countries.

During the past few years Brazil and the United States have made a concerted effort to work together in resolving some difficult bilateral economic issues. I am happy to say that these mutual efforts have borne fruit. They not only resolved the major economic issues outstanding between our countries, but have helped to strengthen overall ties between us as well. Just last week, Secretary Miller and I had the pleasure of meeting with the Planning and Finance Ministers of Brazil to continue the process of close consultation which has produced these results.

As the world enters a new decade, our economic relations will continue to expand and will increasingly focus on the broader role of the United States and Brazil as partners in managing the international economic system. In my remarks today, I would like to share with you some thoughts about possible future directions for the United States-Brazil economic relationship.

### **Global developments**

The prospects for the world's economy as we enter a new decade are stark and sobering. The world economic outlook for both the immediate and longer term hinges on political developments in the Middle East and on oil market developments. Many of the major factors in the outlook are on the pessimistic side. The world as a whole could well see less growth, higher inflation and more external financing problems in the period ahead.

In spite of a weak worldwide growth outlook, inflation rates are rising everywhere. Industrial countries could face double-digit inflation rates during 1980. Less developed countries could see an inflation range of 35-40 percent.

Large external imbalances are also likely. We expect the OPEC surplus to mushroom to something like \$120 billion this year, nearly double last year's surplus. This surplus must be matched by an equivalent deficit for oil importers as a group, the bulk of which will have to be financed by borrowing in world capital markets where OPEC countries are placing most of their surplus funds. We have confidence that the financial system can accommodate the current high levels of oil prices without being severely strained. But we must monitor the situation closely.

A number of countries—both DC's and LDC's—will need to take adjustment action to reduce their deficits and restrain domestic inflation. The International Monetary Fund (IMF) has substantial resources to provide support for such adjustment actions, and will have even more when the latest quota increase becomes effective. It is important that countries initiate adjustment promptly, and go to the IMF at an early stage when necessary.

### **Brazilian development**

From this overview of the world economic outlook, let me turn to a few observations on Brazil. Over the past two decades Brazil has rapidly emerged as a major world economic power. Its impressive growth and development has catapulted it into a position of leadership within the developing world. Brazil's rapid progress has been clearly demonstrated by a broad range of economic indicators:

- Since 1970, Brazil's real GNP has multiplied fivefold (in current dollars) to more than \$200 billion. This represents nearly 20 percent of total GNP of the non-OPEC developing nations. Brazil is the eighth largest free market economy in the world, ahead of many OECD countries on this measure.
- Brazil's annual real GDP growth in the past decade averaged 9.2 percent compared with only 4.9 percent for all developing countries, and about 3.1 percent for the industrialized countries.
- This year, Brazilian exports could reach nearly \$20 billion, or one quarter of the total from all Latin American countries. On a worldwide basis it ranks second only to the United States as an exporter of food products. At the same time, industrial products now represent over 50 percent of total Brazilian exports.



- Brazil's excellent economic record and potential have enabled it to become one of the top five international borrowers in the world and the largest single foreign customer of the United States banks, which now have a total of nearly \$15 billion in outstanding loans to Brazil.
- It is also the largest single borrower from the World Bank and Inter-American Development Bank, which have lent Brazil a combined total of over \$7.5 billion. Through these and other investments Brazil has now developed to the point where it has also begun to assist some of its less fortunate neighbors, as demonstrated by its contributions to the International Development Association and the African Development Fund, as well as by its initiatives in the Inter-American Development Bank to make a larger proportion of its contribution to IDB resources available for less developed countries.
- Brazil now plays host to more than \$15 billion in foreign direct investment, and ranks seventh in the world as a host for U.S. direct investment which now equals more than \$4 billion.

Brazil's enormous progress is not accidental. The "Brazilian miracle" is the result of a sophisticated and prolonged effort to raise the country into industrialized status. Although the road has not always been smooth, Brazil has been uniquely successful in this endeavor. Even during periods of severe international economic difficulty such as in 1974-75, Brazil managed to keep its economy growing at a brisk pace. As a result, Brazil now has the third largest GNP in the Western Hemisphere and is clearly in the vanguard among middle-income countries.

### Common interests

In the present global environment, characterized by profound and rapid economic change, it is increasingly important for nations like Brazil and the United States to recognize their common interests, strengthen their cooperation in managing bilateral concerns, and devise a forward-looking approach in dealing with international economic issues. Some of the critical challenges include promoting an open and growing world trade and payments system, fostering a positive environment for international investment, insuring continued availability of financial resources to LDC's, stimulating the development of alternative energy sources, controlling global inflationary pressures, stabilizing world commodity prices, and insuring adequate rates of growth of global production.

Perhaps the most vivid example of this mutual concern is energy. As major oil-importing nations, the United States and Brazil are now going through a painful transition phase. In 1973, Brazil's oil import bill of about \$1 billion absorbed 14 percent of total export earnings; this year, the total cost of its petroleum imports is likely to approach \$10 billion, or about half of its expected export revenues. Brazil is now the largest oil-importing country in the world outside of the OECD.

By comparison, U.S. oil imports also grew dramatically from \$7.6 billion in 1973 to about \$60 billion in 1979. Now, every 1-percent increase in the price of oil adds over \$800 million to the annual import bill of the United States and over \$100 million to the annual import bill of Brazil.

The United States and Brazil also face considerable challenges in dealing with growing domestic inflationary pressures, while insuring balanced growth. Last year, inflation rates in both the United States and Brazil surpassed levels previously reached in either nation during the 1970's. In attempting to achieve greater price stability and establish better balance in the external sector, our countries face the unfortunate prospect of lower economic growth and the possibility of rising unemployment.

At the same time, both countries are confronted with the prospect of global recession and rising protectionist pressures which could adversely affect our trade flows. As large exporters we must continue to combat these trends if our economies are to grow in a stable and sustainable fashion. It is essential that we work closely together with other nations to maintain an open world trading system. Our governments worked closely together in developing the new subsidy/countervailing duty code; I anticipate that we will continue to work closely in managing future trade problems and implementing the agreements we have achieved.

Similarly, we share a strong interest in developments in the international capital markets. Brazil is one of the world's most prominent borrowers of private credit, as well as the largest client of both the World Bank and the Inter-American Development Bank. It is also a highly attractive market for foreign equity investment which now totals about \$15 billion, the highest among all of the developing countries in the world. The United States, on the other hand, as the world's largest financial market, has been a source of much of these funds, both directly through private bank credits and U.S. business investment, as well as indirectly through the multilateral development institutions to which the United States is the principal contributor.

Our countries both have an important stake in world commodity trade. Together we account for a significant share of trade in coffee, cocoa, soybeans, wheat, and bauxite. Consequently, instability in world markets has a large impact on the U.S. and Brazilian economies. By the same token, policy decisions by either country can have a large impact on world commodity markets. In view of our interest in stable markets, we could both benefit from regular discussions of commodity problems.

### Conclusions

We believe that an effective economic relationship between the United States and Brazil must continue to be based on the twin principles of shared responsibility and increased participation in international economic decisions.

The United States recognizes and supports an enhanced role for Brazil in the international economic system. At the same time, Brazil is considering how it can most effectively translate its enhanced position into both a greater role in the world economy and to insure maximum possible benefits for its own economic development. We believe that these dual goals are mutually consistent. While recognizing that Brazil still must overcome many of the pressing problems facing the developing world such as widespread poverty and uneven income distribution, it can at the same time actively participate in the resolution of global economic issues. The challenge for the future economic relationship between the United States and Brazil is to strengthen and diversify the fundamental basis of our collaboration to deal with the complete spectrum of international economic problems which we both face from our different perspectives but with underlying national interests which are very similar.

Brazil has recently undertaken fundamental adjustments in the management of its economy, which provide a firm foundation for such future collaboration and which mark a clear departure from the past. The policy reform measures announced by the Government in December 1979 and further articulated since then demonstrate Brazil's determination to take comprehensive steps in order to achieve greater price stability and external adjustment. This set of reform measures included a significant liberalization of Brazil's foreign trade regime. The Brazilian Government's action to eliminate immediately its principal export subsidies, raise interest rates gradually on subsidized export credits, cancel the prior import deposit requirements, and revise the Law of Similars further demonstrates its strong commitment to an open world trading system. As a result of these and other actions, a source of earlier trade frictions with the United States and other countries has been finally eliminated.

Brazil has also stepped up its efforts to adjust to the global scarcity of energy resources and reduce its growing dependence on imported petroleum, thereby contributing as well to the global energy balance. Perhaps most notable is its ambitious program to free its 6.5 million vehicles from gasoline and run them on alcohol. The Government has already spent \$2.5 billion on this effort and is budgeting almost twice that amount for the next 5 years.

Reconciling Brazil's desire for continued rapid expansion of the domestic economy with the need to establish better balance in the external sector has not been an easy task. The recent policy measures adopted by the Government should enhance the confidence of foreign investors and lending institutions in the soundness of Brazil's development prospects. Moreover, the successful implementation of these policies should significantly contribute to the continued dynamism of the Brazilian economy and to its ultimate emergence as a full-fledged industrial power. While we recognize that Brazil cannot achieve this overnight, the demonstrated resilience of the Brazilian

economy to internal and external difficulties suggests that with continued perseverance it can readily adjust to new global realities.

There are many areas where the prospects for further collaboration based on policies already undertaken in both the United States and Brazil are bright:

In the trade field, most bilateral problems are now behind us. As Brazil continues to reap greater benefits from world trade, we encourage it to continue to liberalize its trade policies.

Increased interdependence will elevate the need for closer and more active consultations about trends in the world economy. Our discussions with the Brazilian Finance and Planning Ministers last week represent part of an ongoing process to exchange views on important economic and financial issues. We expect that this process will continue to grow in the future.

We believe the possibilities for cooperation in the investment field are also worthy of increased attention. The scope is broad, including issues such as the transfer of technology, taxation of royalties and profits from foreign investment, and the role of official investment incentives and performance requirements. We should together work toward agreement on a common basis for new "rules of the game" for international investment. Given our respective positions as major agricultural exporters, the United States and Brazil have a common ground from which to pursue closer cooperation on commodities trade.

We should also seek closer cooperation in devising innovative solutions to our respective energy needs. While a bilateral framework already exists in this area, we should step up our technology exchanges in the development of alternative sources of energy.

These are only a few of the areas where we can develop a common foundation for further, even closer partnership between the United States and Brazil. I could mention many others such as technology transfer, strengthening the international financial institutions, and so forth. But the pattern should now be clear. Together we can and should serve as constructive forces for remolding the world to accommodate new interests and new realities. Only by such close cooperation can we hope to achieve a peaceful, prosperous, and successful global economic system.

**Exhibit 75.—Excerpts from statement by Secretary Miller, February 26, 1980, before the Subcommittee on Foreign Operations of the Senate Committee on Appropriations, on the administration's requests for the international financial institutions**

We meet this morning to discuss the administration's requests for the international financial institutions in the context of an international situation which is characterized by greater tension in both the strategic and economic sphere than has been the case in recent history.

The tension affecting our strategic interests is most clearly linked to events in Southwest Asia. The revolution in Iran and the Soviet aggression in Afghanistan have heightened awareness throughout the world of the many different sources of threats to peace.

The economic tension stems from the somber global economic outlook. Much of the 1970's was characterized by high inflation, soaring energy costs, low growth rates, and unprecedented imbalances in external payments. Largely as a result of various cooperative efforts, the international community weathered the economic turbulence reasonably well. Nevertheless, adverse oil market developments have again radically affected economic prospects. The reemergence of a large current account surplus in the OPEC countries, projected roughly on the order of \$120 billion for 1980, and the inevitable generation of a corresponding deficit in non-OPEC countries will make serious balance of payments pressures inevitable for a growing number of countries.

Events in the Middle East have driven home dramatically the linkages between foreign policy and economics. We can be successful only if our strategy deals with both the strategic and economic crises which we face, and the interrelationships between them.



The administration response to the increased tensions, in both the strategic and economic arenas, has relied heavily on the international institutional framework which has evolved since World War II. This framework was designed under U.S. leadership to provide a system whereby all countries, large and small, could turn to seek cooperative solutions to their fundamental concerns. In the foreign policy area, we have turned to NATO, the United Nations, and the World Court. Economically, we rely heavily on the institutions which are the subject of today's hearings.

The International Monetary Fund (IMF) and the multilateral development banks (MDB's) are the front lines of defense for the world economy. During the 1970's, they were pivotal factors which both facilitated needed economic adjustments and helped sustain growth: the IMF through its surveillance and oversight activities and also through its expanded and liberalized financing facilities, and the MDB's through their increasingly important role in Third World development.

The distinct but complementary operations of these institutions serve U.S. interests greatly. They will be invaluable assets in facing the growing economic and financial problems of the new decade. The uncertain world economic environment—which the Soviet Union will seek to exploit—makes it all the more important for the United States to assure that the IMF and the MDB's can respond effectively to the needs of their members. In the economic arena, as in the international political and military spheres, the United States cannot maintain an effective leadership role—and assure our national security—unless we are willing to provide resources adequate to the dangers confronted.

The administration's appropriations requests for both the International Monetary Fund and the multilateral development banks are designed to do that.

I am submitting for the record a detailed background paper which deals fully with the administration's request and provides specific material on the operations of the Fund and the banks.

In today's testimony I want to emphasize my conviction that it is absolutely crucial for the United States to continue its strong support for these institutions. They are valuable examples of successful international cooperation. More importantly, they are directly supportive of vital long-term U.S. foreign policy interests. Now is not the time to undermine our influence in these institutions and over global economic developments. The stakes are too high.

\* \* \* \* \*

### **The multilateral development banks**

The United States has an important responsibility in working to establish and maintain an international economic environment which furthers the process of equitable economic growth in the developing countries. This reflects the realities of economic interdependence, in which the prosperity of each nation depends upon the well-being of others. In addition, the countries of the developing world are an increasingly important factor in protecting U.S. security and other foreign policy interests. It is a simple truism to recognize that the prospects for developing country support on global issues of importance to the United States will be enhanced by U.S. cooperation on issues of keen interest to them. In the case of most of the Third World countries, the fundamental concern is development.

Poverty exists on a large and pervasive scale in developing countries throughout the world. There are large gaps between developed and developing countries in terms of living conditions and the quality of life: in health and nutrition, literacy and education, life expectancy, and in the overall physical and social environment. The natural growth of population and the process of industrialization have compounded already immense problems of unemployment and underemployment and fueled a rapid increase in the size of urban populations, most of which are without access to rudimentary health and sanitation services. In addition to new problems generated by this rapid urban growth, the primary concerns in low-income countries—with large numbers of rural poor and heavy reliance on agriculture—remain with the requirements of the rural economy and the need to improve production of the small farmer.

The multilateral development banks (MDB's) are at the heart of international efforts to address these development concerns. They are unique institutions by which the

United States can work cooperatively with developing countries in support of their aspirations for economic and social progress.

The banks have proven themselves to be effective instruments for promoting growth with equity. Last year they made loans totaling nearly \$14 billion which helped to finance 425 projects in 90 developing countries. The banks now account for between 10 and 15 percent of the total external resources moving to the developing world. This proportion is much higher for the poorer countries which do not have access to the international capital markets.

Important as this transfer of resource function is for the MDB's, a far more important contribution to development lies in the way their projects have become the principal catalyst for growth and contributed to rational sector and macroeconomic policies in developing countries. In this regard, they have organized increasing amounts of cofinancing from private as well as from other public sources.

The MDB's also have a key role in the transfer of technology and in providing sound advice on economic policy associated with their lending activity. This contribution to "institution building" and "human capital formation" permeates the process of project implementation and is perhaps the greatest contribution made by the banks to the long-term economic prospects of the developing countries.

It is the combination of project financier, financial catalyst, and institution builder which makes the MDB's such unique and important agents in the development process.

Throughout the history of bank operations, the United States has supported and encouraged those adaptations in bank operations which we believed would further increase the effectiveness of bank lending. Among the more important results of past U.S. initiatives are the shift in the sectoral composition of MDB lending to those sectors such as agriculture and rural development where project benefits accrue more directly to the poor, the use of the MDB's considerable aid leverage to promote policy changes in the borrowing countries which favor the poor, and the recently emphasized step-up of MDB lending to increase developing country energy supplies.

The cooperation among countries within the MDB's contributes significantly to the substance as well as the atmosphere of U.S. ties with developing countries. U.S. participation in the banks also reflects a successful partnership with Europe, Japan, and Canada—with whom we work closely on MDB financing arrangements. Any significant slackening of traditional U.S. support for the MDB's would both seriously jeopardize our relations with the developing world and weaken the confidence of our allies in U.S. ability to play a cooperative role across a broad range of international activities. Undermining such a pillar of the international institutional framework would also make it much more difficult for us to get the support of the developing countries for our positions in other international bodies on issues of central concern to our own national interests.

In this context, Mr. Chairman, we are deeply concerned by the continued failure of Congress to pass the FY 1980 appropriations bill. The absence of this legislation is having a major impact on the MDB's.

The International Development Association (IDA), the Fund for Special Operations (FSO) in the Inter-American Development Bank (IDB), and the Asian Development Fund (ADF) have completely run out of commitment authority and have been compelled to process all new commitments on a contingent basis. The lending program of the African Development Fund (AFDF) may soon have to be curtailed completely. The IDB has already scheduled a special meeting to discuss this situation and the Asian Fund may call a similar meeting soon.

The economic consequences for the developing countries will be severe if MDB lending is not maintained. A number of countries, particularly in Africa, are dependent on the banks for a large portion of their development budget and have already expressed concern to the United States about the cutoff in IDA lending. Some of these countries are of key importance to us right now. Loans to Pakistan and Kenya, among others, are being held in abeyance.

Continued U.S. failure to meet our negotiated shares of MDB financing can only impede our efforts to win widespread support for our own foreign policy and national security objectives. I strongly urge that maximum effort be made to complete final

passage of the FY 1980 bill this week with an appropriation as close as possible to the administration's request.

### **Economic benefits of U.S. MDB membership**

As the administration's chief fiscal officer, I am committed to budget restraint. At the same time, for the reasons I have outlined, the United States must maintain a reasonable program of foreign assistance. The multilateral development banks reconcile these needs.

First, other members contribute \$3 for every \$1 contributed by the United States. Second, supported by callable capital, the banks finance the bulk of their lending program through borrowings in the private capital markets. The result is that U.S. budget expenditures are multiplied many times over in actual MDB lending. For every dollar the United States has paid into the World Bank over the past 35 years, for example, the Bank has lent over \$50. Our development assistance gets maximum leverage when channeled through the MDB's.

In addition, U.S. producers and consulting firms have received the largest share of MDB-financed procurement contracts. This has led to a significantly beneficial impact on U.S. employment and GNP. For every dollar we have paid into the MDB's for the years 1977 and 1978, the U.S. economy has grown by an average of \$3.00. Over the life of the institutions, they have also contributed \$11 billion to our current account.

### **The FY 1981 Appropriations Request and Callable Capital**

For FY 1981, the administration is requesting total budget authority of \$1,666 million for U.S. subscriptions and contributions to the MDB's. The request is based on the assumption that the FY 1980 appropriations bill, as finally approved, will include the higher amount for each of the banks contained in either the House or Senate version. This conforms to OMB's practices regarding all of this year's programs. The FY 1981 request will have to be amended depending on the outcome of the FY 1980 bill. The outlay effect of the request will be spread over time, and thus the request will have only a minimal impact on this year's or next year's budget.

The amount of the FY 1981 request is much lower than that for last year. This is principally because we are not seeking budget authority for the callable portions of our capital subscriptions to the banks. The treatment of callable capital is an issue to which you have rightly called attention, Mr. Chairman, and indicated that a change in budgetary approach would be desirable. Full appropriation of callable capital has been totally out of line with the treatment of other contingent obligations of the U.S. Government.

The "callable capital" concept is one of the most attractive features of the multilateral development banks and results in considerable budgetary savings for the U.S. Government. With callable capital as backing, the MDB's are able to borrow most of the nonconcessional funds they require in international capital markets. The cost to the U.S. Government of subscriptions to callable capital is solely contingent in nature, since callable capital can only be used to meet obligations of the MDB's for funds borrowed or guaranteed by them in the unlikely event that the banks' other resources are insufficient to meet those liabilities.

Even if calls were made, \$11.5 billion has already been funded by the Congress against the potential U.S. liabilities. It is therefore virtually certain that there will never be budget outlays resulting from the subscriptions proposed in the legislation before the Committee. Unlike other donor countries, however, the United States, in its budgetary procedures, has heretofore treated callable capital subscriptions as though they would have an outlay impact.

The issue of changing the appropriations and budgetary treatment of callable capital has been raised by you and other members. The administration has given this matter very careful study and concluded that appropriation for the full amount of callable capital, and the resulting scoring of the appropriated amounts as budget authority, distort the true size of the request for the MDB's.

After consultations with you, Mr. Chairman, and many others in the Congress, the administration therefore proposes enactment of program limitations in the FY 1981 Foreign Assistance Appropriations Act for U.S. subscriptions to callable capital



instead of actual appropriation and budgetary authority. We have also submitted proposed changes in the authorizing legislation which will enable us to make the subscriptions after program limitations are enacted. Full congressional control over callable capital subscriptions is retained, both by the program limitations and because subscriptions to callable capital and paid-in, which must be appropriated in full, generally have to be made in specified proportions. The General Counsel of the Treasury Department issued opinions in 1975 and 1979 that appropriations are not legally required to back subscriptions to callable capital unless and until payment is required of the United States on a call made by an institution.

### **The sixth replenishment for the IDA (IDA VI)**

The background paper submitted for the record details the specifics of the administration's full appropriations request. I would like to highlight two of the larger components of the request: the sixth replenishment for the IDA and our remaining subscription to the special capital increase of the World Bank itself.

IDA expresses the determination of the more advanced countries to reduce, albeit slowly, the problems of absolute poverty in the poorer nations of the world. The 54 IDA borrowers account for approximately 31 percent of the world's population, but only about 3 percent of the global gross national product. Approximately 90 percent of IDA's funds go to countries whose per capita income is below \$300 per year (1977 dollars). Lending is concentrated on those sectors which promise to improve most directly the lives of the very poor.

With few exceptions, IDA recipient countries lack the physical and human resources to adapt quickly to the problems confronting the global economy. Their terms of trade have deteriorated. They have not been able to attract sufficient capital to maintain imports and thus sustain even their already low growth rates. Since 1974, the real value of their imports has declined. As a result, most of the poorest countries achieved per capita growth of only around 1 percent per annum during the 1970's.

Even with a major effort by the poorest countries themselves, additional concessional resources are required to achieve both higher rates of growth and greater progress in poverty alleviation. More than one-third of the total population of the developing world—800 million people—still subsists in conditions of absolute poverty.

After 18 months of negotiation, donor countries reached agreement last December on a \$12 billion IDA VI to permit continued IDA lending for the 3-year period beyond June 1980. Relative to donors' gross domestic products, the size of the replenishment remains at roughly the ratio of IDA V and will thus permit a modest annual growth in IDA lending.

The United States joined other donors in supporting this replenishment noting, however, that our support was contingent on the enactment of necessary authorization and appropriations legislation. The United States insisted on a sharp reduction in the U.S. share. After lengthy negotiation, we achieved a reduction in our share from 31 percent in IDA V to 27 percent in IDA VI. This decline continues the downward trend in the U.S. share of IDA from its initial level of 42 percent, and was accompanied by a substantial increase in the shares of Germany (from 10.9 percent to 12.5 percent) and Japan (from 10.3 percent to 14.65 percent). The reduction of four percentage points in the U.S. share constitutes a very significant improvement in the distribution of responsibility for providing funds for IDA, saving us \$480 million over the life of the agreement.

A U.S. share of 27 percent of a \$12 billion IDA VI replenishment results in an average annual U.S. contribution of \$1,080 million. This represents virtually no increase in real terms in U.S. funding for IDA. Its annual lending rises by a modest amount, but our share declines by 4 percent. All real growth in IDA lending will be financed by other donors.

### **World Bank selective capital**

In 1977, Congress authorized United States participation in a selective capital increase (SCI) for the IBRD. The United States has been behind in its scheduled SCI payments since the first installment, however, and the shortfall now totals \$200 million, assuming the Senate level for FY 1980 (i.e., \$825.8 million) is agreed. A

subscription of the full amount would require only \$20 million in budget outlays, since 90 percent of our subscription represents callable capital.

Reluctance to meet our full SCI subscriptions is ironic because the Bank's great success is to a large extent due to the leadership the United States has provided in the Bank since its creation in 1946. The shortfall in U.S. funding is particularly inopportune now that the Bank, at U.S. initiative, has mounted a major program to increase world energy supplies. The World Bank's energy program will grow to at least 15 percent of total Bank lending within 5 years. It will amount to \$7.7 billion over the period for the exploration, production, and development of oil, gas, and coal, and for the construction of new hydroelectric facilities. In operation, these Bank projects will produce additional primary energy estimated at 2 to 2.5 million barrels of oil a day, thus reducing by that amount potential world demand for OPEC oil.

A U.S. failure to complete our SCI subscription could lead other members to insist on a significant cutback in the Bank's annual lending program because doubts would be generated about U.S. support for Bank lending throughout the 1980's. Such a cutback in the lending program would be disastrous for our relations with the developing world, undermining Bank programs in countries and regions of particular concern to the United States (e.g., Egypt, Turkey, the Caribbean, and Central America) and heightening international monetary problems by increasing demand on private capital markets.

Subscription of the full SCI amount is also essential to maintain U.S. voting strength above 20 percent and thus protect the U.S. veto in the Bank. The veto ensures that no changes are made in the Charter which would have a detrimental impact on U.S. interests.

### **The African Development Bank**

The U.S. subscription to the African Development Bank (AFDB) is an important new component of the FY 1981 appropriations request. Subject to receiving authorization for U.S. membership in the bank, an initial appropriation of \$18 million is being sought.

Membership in the AFDB to date has been restricted to African nations. The limited resources of the African members have, however, severely restricted the Bank's access to the private capital markets and its lending program. As a result, in May 1979, the Governors of the Bank invited nonregional countries to join. The proposed U.S. subscription would represent 5.68 percent of the AFDB's total capital and 17.04 percent of the nonregional subscription.

The United States has direct economic, humanitarian, and political interests in assuring a strong and viable Africa where poverty is reduced, the pace of economic growth accelerated, and serious financial problems avoided. While a wide range of U.S. political and economic policies already contribute toward these objectives, our membership in the AFDB, the most prominent pan-African development institution, would help strengthen our ties with African nations and meet our growing interests in the region.

### **Other regional MDB's**

The remainder of the administration's request is for appropriations for capital subscriptions and contributions for the Inter-American Bank (IDB), the Asian Development Bank (ADB) and Fund (ADF), and the African Development Fund (AFDF):

- \$51.6 million in paid-in capital for the IDB and \$318 million for the Fund for Special Operations, the IDB's concessional lending window;
- \$25.2 million in paid-in capital for the ADB and \$111.2 million for the ADF, the bank's concessional window; and
- \$41.7 million for the AFDF, which provides concessional financing for Africa's poorest countries.

These regional institutions were established to complement the activities of the World Bank group and increase the direct involvement of the recipient countries in the development process. They now provide a central element in the development

strategies of many friendly nations, and are uniquely positioned to bring to bear a special regional expertise to local problems. The regional MDB's also facilitate the mobilization of additional resources from the developing countries themselves.

## Conclusion

In conclusion, Mr. Chairman, I would like to reemphasize my strong conviction that the International Monetary Fund and the multilateral development banks are essential to U.S. interests.

The international monetary system is undergoing a period of major change and potential strain. The IMF is our central institution for monetary cooperation, and an important source of strength, stability, and broad direction as we try to contend with these changes. We need to recognize, of course, our own continuing large role in the world economy, and our responsibility for maintaining a strong U.S. economy and a sound dollar. But we need also to understand that a strong IMF role in guiding the system is of direct importance to our own efforts to strengthen the economy and maintain the integrity of the dollar. In strengthening the IMF, the United States will be making an important contribution to an international environment which greatly facilitates effective foreign policy. We will also be strengthening a source of balance of payments financing on which we are eligible to draw.

The multilateral development banks are the most effective instrument for promoting economic growth and political stability—and hence U.S. interests—in the developing world. They encourage sound national economic policies and provide an effective framework for bringing the developing countries into the open market system we espouse. Moreover, the banks give us good value for our money with U.S. budgetary expenditures multiplied many times over in actual bank lending. They benefit borrowers and lenders, developing and developed countries alike. The importance of the banks has been reinforced by the fact that recent economic difficulties have exposed a number of developing countries to serious threats of political, economic, and social instability.

The problems we face have a direct bearing on our national security interests. The problems are difficult but not unmanageable. Given a reasonable degree of international cooperation, we have the resources to assure a gradual expansion of the world economy. Healthy and growing economies strengthen the foundation of our international economic system, and maintain an environment conducive to multilateral cooperation on a broad range of other issues critical to the United States.

The seriousness of the current world situation leaves little doubt about the importance of a sound international structure for dealing cooperatively with vital issues. Now is clearly the time for renewed U.S. leadership in support of the Fund and the multilateral development banks and the mutually beneficial endeavors which they represent. For this reason, the administration urges Congress to provide the necessary funding to sustain the operations of these institutions and encourage their pivotal role in building a cohesive and stable world.

**Exhibit 76.—Excerpts from remarks by Deputy Secretary Carswell, April 15, 1980, before the 21st annual meeting of the Inter-American Development Bank, Rio de Janeiro, Brazil, regarding U.S. support for the Inter-American Development Bank**

It is a special pleasure to be here in Rio de Janeiro to address this distinguished group on the 20th anniversary of the first meeting of the governing body of the Inter-American Development Bank. I would like to join my colleagues in reaffirming our strong support for the Bank, its able President, Antonio Ortiz Mena, and our commitment to continued progress in achieving balanced and equitable growth through the hemisphere.



\* \* \* \* \*

## World economic situation and outlook

The prospects for the world's economy as we enter a new decade are sobering. The problems of the last several years not only remain but will intensify and place added stress on the cooperative international structure which has served the hemisphere well since the end of World War II.

\* \* \* \* \*

The current world economic outlook for slower growth, soaring oil prices, high inflation and heightened investor caution has inevitably affected the economies of Latin America and Caribbean countries as well. Inflation averaged, for example, more than 50 percent in Latin America last year, and the region's current account deficit increased from \$15.8 billion to \$20 billion over the same period. These and other economic difficulties will require some adjustment over the next several years. They also make clear the critical importance of the long-term development assistance provided by the Inter-American Development Bank and the other multilateral development banks during this difficult period.

## U.S. overall situation

In the last 6 weeks the administration, the Federal Reserve, and the Congress have made a concerted and unprecedented effort to address the critical issues of inflation, energy development and conservation, and slow growth in our economy. \* \* \*

\* \* \* Key elements of a coherent energy program have been, or are about to be, enacted by the Congress, and by the end of 1981, oil prices in the United States will have been fully decontrolled. This program will produce results and may well be the most important contribution the United States can make to improve the economic well-being of Latin America, given the high degree of economic interdependence between our two regions. But it will require discipline and sacrifice in the United States of popular capital and social programs. In that climate of fiscal austerity, it has been and it will be difficult to achieve full support for foreign assistance programs.

But despite the austere economic climate, in his revised budget, the President has protected the development bank legislation from cuts and has made it clear he will maintain strong, undiminished support for Latin American development, the Bank, and the fifth replenishment.

\* \* \* \* \*

## Latin American outlook in the 1980's

The record for Latin America and the Caribbean over the past two decades that span the work of the IDB shows clear progress. During the 1970's the Latin American economy as a whole continued to expand at a rapid pace and showed remarkable resiliency. Last year regional GDP grew by 6.5 percent, culminating a decade during which average annual growth was 5.9 percent. This compared with a 3.5 percent a year expansion rate for developed countries as a group. Over this period per capita income rose from \$970 to \$1,400, and the area has become much more industrialized. At the same time, Latin America's importance in the world economic system has grown, and we expect this trend to continue during the 1980's. This dynamic growth is a consequence of many factors: improved understanding of the development process, improved planning and administrative capabilities, as well as improved access to capital. These factors should provide the basis for continued progress in the years ahead despite the strained world economic conditions we presently face.

Over the longer term, however, Latin America and the Caribbean will face some major challenges. With an estimated 30 percent of the population still living in desparately poor conditions, widespread poverty remains a major problem. In addition, unemployment and underemployment combined are as high as 40 percent in some countries. A concerted effort is still required to improve the distribution of income both within and among countries and to ensure more efficient utilization of domestic resources.

While impressive gains have been made in many sectors in Latin America, it is disturbing to note that similar progress has not been made in increasing food production. Poverty and food shortages mean hunger and poor nutrition for millions of people in the hemisphere. That condition is not acceptable to any of us.

We believe that these problems must be met directly and that increased attention must be devoted to them in the years ahead. We expect that the Bank, with its technical expertise and substantial capital resources, will play an important role in this.

### **The Inter-American Development Bank**

Over the past 20 years, the Inter-American Development Bank has played a vital role in assisting Latin American and Caribbean countries in achieving the major goal of balanced development with equity through regional cooperation. Through its lending and technical assistance programs, the Bank has helped to increase member countries' production capacities, strengthen national and regional institutions, improve social services and increase agricultural production. It also has been a catalyst in mobilizing additional domestic resources and attracting additional private external capital to the region.

To a great extent, the success of the IDB's development activities has been due to the Bank's ability to respond to the changing conditions in the region and to find innovative means of fulfilling the region's developmental and capital needs. Over the years, the Bank has been a well-known pioneer in the fields of land reform, integrated rural development, public health, and urban development. In recent years, it has broadened its membership and expanded its capital base, reflecting its increasing capital needs and its increasingly important role in the world economic system.

The United States believes that the fifth replenishment agreement establishes a sound framework through which the Bank will be able to continue and to heighten its contribution to development in Latin America and the Caribbean during the 1980's. We are also encouraged by the extent to which the Bank has already moved to implement the terms of the agreement.

Perhaps the most important aspect of the fifth replenishment agreement is the Bank's new policy for devoting 50 percent of its resources over the 1979-82 period to low-income groups. This policy reflects the conviction of the members of the Bank that in order to attain our goals of broadly based economic and social development, we must devise new ways to reach those who have not fully shared in the fruits of economic and social development in the past. In our view, this must also include a commitment to ensure that all citizens of this hemisphere are accorded their basic human rights and dignity as individuals. This is essential not only to promote justice in the hemisphere, but also because the ultimate success of countries' economic development depends on it.

We also recognize the substantial contribution which the higher income countries are making to assist their poorer neighbors. Because of their cooperation in the fifth replenishment, the Bank is better able to direct its resources where they are most needed and thereby do the most to promote more equitable growth in the hemisphere.

The United States would also like to commend the Bank's efforts in the field of energy. With soaring oil costs contributing to severe inflation and balance of payments problems, expansion and diversification of the world's energy supplies are vitally important. The IDB is contributing toward the achievement of that goal by devoting a substantial portion of its lending to energy projects. About one-quarter of the Bank's lending was devoted to the energy sector over the past decade. We are pleased that the Bank will continue to devote a similar proportion of its lending program to this critical sector in coming years. Beyond its activities in traditional energy fields, we believe the Bank should expand lending and technical assistance in other energy-related areas such as improved energy planning, pricing policies, and conservation, the exploitation of renewable nontraditional energy resources, and the development of promising new technologies.

In addition, it is important that the Bank examine further possibilities for mobilizing external resources for the energy and minerals sectors. Substantial private and public investment will be required to develop the potentially large untapped energy and mineral reserves of the region.

In reviewing some of its achievements in recent years, it is clear that the Bank has made a consistent and concerted effort to address and resolve some of the principal development problems confronting the region. Many of these problems will persist into the 1980's, and new challenges will undoubtedly arise. The forthcoming study of the role of the Bank in the 1980's should help identify the major challenges which lie ahead and suggest ways in which the policies established for the fifth replenishment period can be refined to meet those challenges more effectively.

Two related problems, which will continue to require close attention over a sustained period of time, are inadequate food supply and rapid population growth. In a majority of Latin American countries, inadequate progress has been made in increasing agricultural production over the last 15 to 20 years. In fact, many countries in the region are producing less food per capita now than they did 20 years ago. The Bank is aware of this problem, and has taken steps to help increase food production; in 1979, it devoted a third of its lending to the agricultural and fisheries sector. We hope that the Bank will continue to provide a substantial amount of resources for constructing and improving the infrastructure and techniques in this sector so that this disturbing trend in the region's food supplies can be reversed.

Related to the problem of providing adequate food supplies and improving living conditions are the implications of rapid population growth. Population in Latin America has been increasing at a rate of about 2.8 percent per year over the last two decades. Most countries recognize the seriousness of this problem, and the Bank should give increased attention to ways in which it can assist its members in this area.

It will also be important to integrate women more fully in the development process. Moreover, the success of countries' efforts to curb population growth will depend in part on improving the economic opportunities for women.

\* \* \* \* \*

**Exhibit 77.—Excerpts from remarks by Secretary Miller, May 14, 1980, before the Chicago Council on Foreign Relations, Chicago, Ill., entitled "The International Financial Institutions: A Critical Role for the 1980's"**

I welcome this opportunity to discuss key U.S. interests in the international financial institutions and the role of those institutions in assuring world economic stability and progress in the 1980's. \* \* \*

The world economy faces dual challenges over the next few years: To assure adequate financing of the huge payments imbalances arising from the major oil price increases that have taken place since 1978; and to promote fundamental adjustment to the changed world energy situation which is at the heart of global economic difficulties. The International Monetary Fund and the multilateral development banks are central to the international community's effort to meet these challenges. Whether the institutions succeed in restoring a strong and stable global economy has a critical and direct bearing on the economic well-being of the United States. The health of the world economy directly affects markets for the production of our farms and factories and for the employment of our labor. In hard times such as we are experiencing now, there is always a temptation to retrench, to cut back on our support for international organizations that seem to have no domestic constituency. This would be a tragic mistake. Our stake in a healthy world economy is strong and growing stronger.

The dependence of the United States upon world trade and financial flows has become enormous. Export markets constitute a major source of demand for U.S. goods and services. Today, one out of every seven U.S. manufacturing jobs and 1 out of every 3 acres of U.S. farmland produce for export. Imported goods, ranging from raw materials to highly sophisticated capital equipment, are thoroughly enmeshed in all phases of U.S. economic activity. International investment has become a major factor in U.S. production, both at home and abroad. The U.S. and international capital markets are highly integrated, and the dollar serves as the principal vehicle for trade and finance internationally as well as domestically.



More than most States, Illinois demonstrates the central importance of the world economy as a market for U.S. products. Illinois is our third largest exporter of manufactured goods and our top exporter of agricultural products. \* \* \*

\* \* \* \* \*

The dramatic oil price increases of the past year are causing a slowdown in world economic growth, a surging of inflation, and sharp deterioration in the balance of payments position of the oil-importing world. Today's world economic environment is likely to make it not only more difficult for nations to obtain needed financing, but more difficult also for them to make the economic adjustments required by changed external circumstances.

\* \* \* \* \*

Thus over the next few years the world faces a dual task of assuring not only that financing is available in adequate amounts, but also that basic economic adjustments are initiated—and carried through—to restore a sustainable basis for future world economic growth and development.

The need for a coordinated approach to these tasks is recognized by the international community. The IMF and the multilateral development banks are at the forefront of efforts to carry out that approach. The IMF is positioning itself to meet potentially large demands for balance of payments financing and to assist countries in undertaking longer term programs to revitalize their economies. An increase in IMF quotas is now in process and the Fund is considering the possibility of borrowing additional funds from major surplus countries should the need arise. Also, the Fund is moving to lengthen the horizon of its adjustment programs in appropriate cases, and to place greater emphasis on expanding and rationalizing the productive base in borrower economies, in recognition of the structural nature of some of the changes that must be made in its members' economies. These efforts by the IMF closely parallel a major initiative being undertaken by the World Bank to promote and support structural adjustment in the developing nations.

The Bank has initiated, with strong support from the United States, a new program of nonproject lending in the form of sequential loan agreements over a medium-term period, perhaps 5 to 7 years. Disbursement of the loan segments, and decisions on subsequent loans in the sequence, would be conditioned on various identified micro- and macro-economic policy changes by the borrowing country, designed to produce "structural adjustment" (especially in response to the changing energy supply situation) in its economy. We are supporting this Bank initiative as an important and necessary complement to its regular practice of project lending.

By cooperating closely in implementing these programs, the Fund and Bank can support efforts of their member countries to undertake difficult adjustments, which necessarily have a medium-term horizon, while simultaneously addressing their shorter term external financing needs. At the same time, it is essential that flows of development assistance, both bilateral as well as through the development banks, be sustained to permit the development process to continue during this difficult period of adjustment.

Major steps are underway to strengthen the resources of both the IMF and the multilateral development banks to enable them to carry out these tasks. It is in the national interest of the United States to participate fully in these efforts. Let me discuss them in turn.

### International Monetary Fund

The purpose of the International Monetary Fund is the maintenance of a strong and orderly international monetary system. It is a revolving fund, from which all participants benefit directly. It is not foreign aid. It is not commodity financing. It is unique, not like any other institution in which the United States participates.

The IMF has two basic functions. The first is general guidance over the operations and evolution of the international monetary system. The second, closely related, is provision of temporary financing in support of adjustment programs by IMF members facing balance of payments problems.

The IMF provides a source of funds, provided by all member nations and available to all through assigned quotas, for supporting countries in their efforts to overcome balance of payments difficulties. A 50-percent overall expansion of quotas—from about SDR 39 billion to SDR 58 billion or, in dollar terms, from about \$50 billion to \$75 billion—has been agreed upon as a key element of the international community's response to increasing and potentially major world balance of payments problems. The IMF has periodically required increases in its resources, in response to rapid growth of world economic activity and international trade and financial transactions. Today, at a time when world payments imbalances and potential demands on the IMF are rising sharply, quotas represent barely 4 percent of world trade as compared with 12 to 14 percent during the 1960's. To maintain a strong IMF, capable of encouraging needed adjustment and providing the temporary financing required to maintain monetary stability, we must assure that its resources are adequate to meet potential needs.

Quotas are central in the IMF. They are its permanent resources. They determine the amounts of financing which countries can draw in time of need. They determine the distribution of SDR allocations. And they determine voting power. Because of these important advantages, nations compete for increases in IMF quota shares, rather than trying to reduce their shares as they do in many other international institutions. The United States has by far the largest IMF quota, the largest share of votes and the largest potential access to IMF resources. Over the years, the United States has drawn about \$7 1/2 billion in foreign currencies from the IMF, second only to drawings by the United Kingdom.

In support of the general IMF quota increase, the administration has requested congressional approval of a 50-percent increase in the U.S. quota, amounting to SDR 4.2 billion or about \$5 1/2 billion at current exchange rates. The proposed increase in the U.S. quota will maintain our share intact at 21.5 percent of total IMF quotas, and thus will preserve our voting position and ability to influence key IMF decisions on the nature and operations of the international monetary system.

### **The multilateral development banks**

The multilateral development banks (MDB's) have received strong, sustained U.S. support throughout their 35-year history. Active, undiminished support during the 1980's will be critical to fundamental U.S. economic, political, and security interests.

MDB loan commitments represent by far the largest official source of external capital for the developing world, equivalent to \$14 billion in 1979. These loans contribute in a major way to economic growth and stability in recipient developing countries. Economic growth in the developing countries is an important U.S. objective, both in terms of basic humanitarian concerns and as a source of strength to the global economy as a whole. The developing nations are today, at a time of a general slowdown, the main area of world economic growth. Growth generates increased imports; and nonoil developing countries now take 20 percent of total U.S. exports, 25 percent of our exports of manufactured goods, and support more than half a million U.S. manufacturing jobs.

In providing policy advice, preparing development projects based upon objective economic criteria, and serving as a financial catalyst, the MDB's are an important and respected force for the development of an efficient, responsive international market economy. They play a key role in the transfer of technology and in "human capital formation" which represent perhaps the greatest contribution to long-term development.

The MDB's also provide an important forum for cooperative efforts among developed and developing countries to respond rapidly to critical world needs. Most recently, this has produced initiatives in two key product areas and, as I noted earlier, structural adjustment:

- The United States has actively supported a shift in the allocation of MDB lending away from infrastructure projects toward agricultural and rural development, and subsequently toward education, health, and population projects as the banks increasingly have adopted a basic human needs strategy to target project benefits directly for the poor. The World Bank is far and

away the largest single source of external funding for agricultural and food production, providing over 40 percent of all official commitments to agriculture. Over the 5 years just ended, total lending commitments for these projects equalled \$11.6 billion, representing 33 percent of total lending. The World Bank expects to finance projects which will contribute on the order of one-fifth of the increase in annual food production in its developing member countries in the 1980's.

- With strong support from the United States, the World Bank plans to finance oil and gas projects which, combined with other official and private financing, will total more than \$33 billion over the next 5 years. This effort should ultimately yield an additional 2.5 million barrels of oil equivalent a day. By increasing world energy supplies, this will help reduce pressures on world oil prices as well as deal directly with one of the most critical bottlenecks to development.

At the same time, increased U.S. support for the multilateral development banks is fully consistent with the need for budget restraint. Indeed, U.S. participation in the MDB's is the most cost-effective approach available to providing development assistance. We derive significant fiscal advantages because the provision of development assistance is shared with other countries, developed and developing alike, and because the MDB's leverage our paid-in contribution through substantial borrowings in world private capital markets.

Also, increasing amounts of our contributions are provided through callable capital, not a penny of which has ever left the U.S. Treasury. Burdensharing and use of callable capital provide the perfect cost-effective combination for our national concern for fiscal prudence. As a result of that combination, the World Bank lends approximately 50 dollars for each and every dollar paid in by the United States.

Finally, through the contributions of other MDB donors and the use of callable capital, MDB loans result in expenditures on U.S. goods and services well in excess of U.S. contributions to the banks. From the inception of the banks through 1978, the cumulative current account earnings of the United States directly attributable to MDB activities totalled \$11 billion, as compared to cumulative U.S. paid-in contributions to the banks of \$7 billion. This net balance of payments benefit is further multiplied within the U.S. economy and generates additional income, employment, and Federal Government and local tax receipts.

Indeed, our analysis indicates that during 1977-78, every dollar contributed to the MDB's resulted in an increase of U.S. GNP of 3 dollars. Total U.S. GNP growth directly attributable to MDB activities averaged \$2.7 billion during this period, raising net Federal tax receipts by \$720 million annually and reducing the net cost to the Federal budget for our participation in the banks to roughly \$170 million each year. If increased local tax receipts were included, the net cost to the American taxpayer would be minimal.

Several U.S. administrations have supported a more equitable sharing of international assistance provided through the development banks. This administration has supported that concept, as a fair assumption of increased responsibilities by other nations in response to today's more pluralistic global economy. As a result, the U.S. share is declining in every MDB in which we have participated since the 1960's.

We must, however, be careful not to travel this path too far. The United States must continue to play a substantial role in the MDB's, not only because of the broad benefits we derive but as a measure of cooperation. It is a simple truism that if we do not support other nations in achieving their major economic objectives, we cannot expect their cooperation in achieving ours.

I must point out, in this connection, that the United States faces at this moment a growing problem, of our own making, which threatens the continued operation of these crucially important institutions. That is the failure of the U.S. Congress to deliver on commitments made by the United States in support of these institutions. The United States is now over \$2 billion in arrears in its contributions to the multilateral development banks. At this point Congress has not yet passed last year's authorization and appropriation legislation for the banks. The result is a complete halt in lending by the Inter-American Development Bank and the Asian Development Fund. Passage of this legislation is urgent.



## Conclusion

Energetic U.S. support for the International Monetary Fund and the multilateral development banks is in our basic self-interest. These institutions are the centerpiece of our efforts to restore stability and growth to a troubled world economy, strengthening the foundations for broad political cooperation. The proposed increase in IMF quotas will help to assure that the IMF can continue to meet its responsibilities for international monetary stability in a period of strain, danger, and financial uncertainty. Our contributions to the multilateral development banks provide the most cost effective means of supporting U.S. humanitarian, economic, and foreign policy objectives in the developing nations, while directly benefitting U.S. exports, production and jobs.

Legislation to support these institutions is now before the Congress. Senator Stevenson and Senator Percy have recognized the major U.S. interest—and that of Illinois—in the international economy, and have given their strong support to this legislation. I welcome their support and hope my comments this evening will encourage yours as well.

### **Exhibit 78.—Excerpts from remarks by Secretary Miller, September 4, 1980, before the Economic Club of New York, New York, N.Y., entitled “The International Financial Institutions: A Time to Recognize U.S. Self-Interest”**

It's a pleasure to meet with this distinguished group to discuss a matter of central importance to U.S. interests: our participation in the international financial institutions, the International Monetary Fund, the World Bank group and the regional development banks.

The 1980's will be a period of great economic challenge and opportunity for this Nation. If we meet the challenge in a forthright and courageous way, we can ascend to even higher levels of prosperity; if we do not, we will slip into a steady decline to economic mediocrity. The program announced by President Carter on August 28 will put us on a course to revitalize our economy through increased investment and higher productivity. We are also taking strong steps to increase U.S. competitiveness in world trade.

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The development banks have received strong, sustained U.S. support throughout their history. Active, undiminished support during the 1980's will be critical to fundamental U.S. economic, political and security interests.

\* \* \* \* \*

\* \* \* the international institutions, with strong U.S. leadership, are moving forcefully in directions that are essential to maintenance of a strong and stable world economy and are directly in the U.S. interest. But there is a potentially critical weakness in this approach. And that is the fact that the United States, whose full participation above all is needed for the institutions to carry out their tasks, is falling seriously behind in providing financial support.

U.S. arrearages to the multilateral development banks have been increasing in recent years and now exceed \$1.3 billion. We are the only major contributor in this position. We are behind because we have not been able to obtain full and timely congressional approval of our requests. For example, legislation authorizing U.S. participation in providing additional funds to the Inter-American Development Bank was needed to bring into effect the agreement by all of the donors to provide funding. Although such legislation was submitted to the Congress in January 1979, there were lengthy delays and the bill was not signed into law until June 1980. As a direct result of these U.S. delays, the Bank was forced to suspend all new lending operations. That suspension affected every developing country in this hemisphere, including such key nations as Brazil and Mexico, and posed particularly severe problems for the smaller countries of Central America and the Caribbean.

Similar delays in passing authorizing legislation for the Asian Development Fund halted concessional lending by that institution to some of the poorest countries in the

world such as Pakistan, Nepal and Bangladesh, and interrupted lending programs for key U.S. allies such as Thailand and the Philippines. Indeed, at the very time the West was trying to respond to the Russian invasion of Afghanistan, all ADF lending to Pakistan was being held up by our legislative delays, effectively blocking more than \$250 million that was in the pipeline. As of June 30, 1980, the midpoint of its fiscal year, the Asian Development Fund had been able to make new loan commitments of less than 8 percent of its program for the entire year.

Legislative delays in our contribution to the sixth replenishment of the International Development Association (the World Bank's concessional lending window) are now preventing the entire replenishment agreement from taking effect.

The Congress is now considering major legislation to increase the U.S. quota in the IMF, to authorize U.S. participation in the sixth replenishment of IDA, and to fund this year's contributions to the multilateral development banks. Failure by the United States to participate fully and promptly in these funding programs would not only jeopardize their lending operations; it would disrupt our own strategy to deal with the most serious world economic crisis of the post-World War II period.

The fact is that this country has come to take for granted a world economy hospitable to its own interests. To be sure, there has been economic tension and instability in the past. Yet, because it has been handled with relative ease and efficiency, we have tended to assume that stability and order were the natural state of affairs. We have allowed our support for the institutions—designed to assure that stability and order—to erode.

We can no longer afford this assumption and neglect. We must recognize our own strong self-interest in actively providing needed financial support to the institutions as they confront the problems of the 1980's.

\* \* \* \* \*

The international financial institutions, with strong U.S. support and leadership, are positioned to guide the international effort. But a potentially major threat to this effort is our own failure—a failure to recognize our own self-interest—to provide full and timely financial support for the institutions. This must be corrected. The world community has charged the institutions with enormous tasks. They need the resources to do the job.

\* \* \* \* \*

### International Economic Analysis

**Exhibit 79.—Excerpt of remarks by Deputy Assistant Secretary Karlik, December 6, 1979, before the Conference Board, New York, N.Y., entitled "Trends in U.S. International Economic Policy"**

The last month of 1979 offers a good vantage point from which to review changes in U.S. international economic policy during the 1970's and to anticipate problems decisionmakers are likely to be confronting during the 1980's. \*\*\*.

In surveying international economic policy trends one can review the spectrum along functional lines such as monetary, trade, investment, and aid policy, or geographically in terms of U.S. relations with specific countries or groups of nations. \* \* \* \* \* During the past year it has become dramatically evident that whenever the Federal Reserve resolves to pursue a particular monetary policy, the Executive a specific budgetary and fiscal policy, or the Treasury a given approach to a financially beleaguered municipality or manufacturing corporation, these decisions have major international economic consequences.

Indeed, at times the pressure of international economic problems has forced modification of what a decade ago would generally have been viewed as exclusively domestic economic policies—policies to be determined solely according to the internal condition of U.S. economy. \* \* \*.

The growth of pressures to lay aside nationalism in the formulation of virtually all U.S. economic policy is the most fundamental change that has occurred in the 1970's, and a trend that is sure to intensify during the 1980's. \* \* \*.

\* \* \* \* \*

### Exchange rate and monetary policy

The world entered the 1970's with the adjustable peg exchange rate system established at Bretton Woods. \* \* \* Canada, in May 1970, was the first major country to adopt, in this case once again, a flexible exchange rate determined essentially by the interaction of market supply and demand. Germany was next, about a year later, and the United States followed in August 1971. There was an attempt to return to fixed rates resulting from the December 1971 Smithsonian monetary agreement, but this collapsed in February 1973.

Agreement on amending the IMF Articles to give members latitude of choice in selecting the exchange rate regime each desired to follow was reached at the January 1976 Jamaica meeting. \* \* \* Since the collapse of the Bretton Woods system, numerous smaller countries have chosen to peg their currencies to that of a major trading partner or to a basket of foreign monies. Nevertheless, today less than 20 percent of global trade moves across pegged exchanges. \* \* \* Changes in U.S. policy attitudes on monetary issues have occurred regarding three important questions: the  $n$ th country problem, the appropriate amount of official intervention, and relations with the IMF.

The  $n$ th country problem arises because, for example, if in a world of a hundred countries, 99 decide individually their dollar exchange rate, then the value of the dollar in terms of all other currencies is fully determined. The United States has no latitude for maneuver, whether or not that exchange rate structure seems appropriate from the U.S. point of view. \* \* \* \* \* The dollar has fluctuated since March 1973; it appreciated until September 1977, then depreciated through 1978, and in 1979 has appreciated. \* \* \* But exchange markets have not demonstrated a capacity to maintain equilibrium exchange rates through smooth changes and without over-shooting or excessive volatility. Thus, intervention is required. In the last 2 years there has been a gradual shift in U.S. official attitudes toward more intervention—a shift sustained by a similar change in attitudes within the academic community regarding the stability of exchange markets and the utility of official intervention. There is no disposition on the part of U.S. monetary authorities to return to a par value for the dollar or to hold the dollar within a specified range of values with respect to a given standard. It is also recognized that exchange rates must change in response to differences among countries in rates of inflation and in the growth of productivity and output. \* \* \* This constraint was believed to stem largely from the dollar's link to gold and, hence, its reserve-asset function. But flexible rates have brought no diminution in the dollar's reserve-asset role. In fact, the proportion of dollars in total reserve has remained at about 80 percent. Given the tripling of global reserves in the 1970's, from 79 billion SDR in 1969 to over 280 billion SDR this year, as opposed to the 38 percent increase in the 1960's—an acceleration of reserve growth that was not supposed to have occurred with flexible exchange rates—the virtually constant proportion accounted for by dollars implied a huge absolute increase in dollar reserves.

From these developments it is evident that the U.S. role in the international monetary system stems from this country's size and its integration into the structure of international trade and investment, rather than from the particulars of how exchange rates are determined and managed.

\* \* \* \* \*

IMF surveillance embodies a major opportunity for closer coordination of economic policies among the leading industrial nations towards mutually agreed goals. \* \* \*

This country has proposed several steps to strengthen IMF surveillance. These include procedures for measuring individual country performance against agreed global standards; requiring countries with large imbalances, surplus or deficit, to submit for IMF review an analysis of how they propose to deal with the imbalances; a more active role for the IMF Managing Director in initiating consultations with members; and establishment of a Governors Council with decisionmaking powers to replace the advisory Interim Committee. \* \* \* \* \* A number of important steps have been taken to promote the SDR. It has replaced gold as the central unit for the IMF,



serving as the numeraire for the system and the unit of account and vehicle for many IMF transactions. \* \* \* The interest rate on the SDR has been brought more in line with market rates and the number of transactions in which SDR may be used have been expanded, thus improving the SDR's ability to compete with other reserve assets.

The IMF is now considering the establishment of a substitution account under which dollars and possibly other currencies could be exchanged for SDR-denominated assets. \* \* \*.

The United States believes that the development of a substitution account could offer a number of attractions for the international community in general. \* \* \* A substitution account could provide an internationally sanctioned, nondisruptive means for countries to achieve a desired reserve portfolio composition without having to hold a number of national currencies. \* \* \*.

There are, however, many difficult questions in the construction of such an account and on sharing the costs associated with operating it. For example, questions must be answered concerning the interest rate and liquidity of the assets issued by the account, the investment of the dollar deposits and the amount and use of interest earnings, and measures to maintain the capital position of the account. \* \* \*.

### Capital flows and investment

During the 1960's the concern about chronic payment deficits, calculated first on a liquidity and later on an official settlements basis, led to the introduction of a phalanx of restrictions on capital outflows. \* \* \*.

All of these constraints have been eliminated. Moreover, at the beginning of this administration a review of U.S. policy towards both inward and outward investment produced a reiteration of the traditional U.S. stance of not inhibiting international capital flows in either direction, and of neither encouraging nor discouraging investment by Americans abroad and by foreigners in the United States. \* \* \*.

The benefits of freedom of capital flows have, in my opinion, demonstrated during the last decade the soundness of this policy. The fears of 1974 that OPEC would buy out the New York Stock Exchange have proved groundless. Instead, banks in the United States, Europe, and Japan have provided an essential service towards maintaining global economic growth by recycling OPEC deposits to countries with temporary balance of payments financing needs. In addition, partly as a consequence of the depreciation of the dollar since mid-1977 with respect to the German mark and the Japanese yen, but also attracted by growth and stability in the U.S. economy, annual foreign direct investment inflows have grown from \$1.5 billion in 1970, and less in 1971 and 1972, to \$6.3 billion in 1978. Such direct investment tends to bolster the dollar in exchange markets and brings the benefits of additional employment, modern technology, and managerial innovations to the United States.

The rapid growth of the Eurocurrency market and the international credit flows it has financed have been a subject of concern to officials for several years \* \* \*. The question here is not one of introducing controls over international flows of liquid assets; rather the issue is whether authorities should and can regulate the growth of credit provided by the Eurocurrency market through the introduction of reserve requirements, mandatory asset-to-capital ratios, or much closer coordination of monetary policy.

The Eurocurrency banks played a critical role in assisting small OECD and developing nations in adjusting to the sharp 1973-74 increases in oil prices. But it is also possible, even though the precise extent of the impact is virtually impossible to determine, that more recent expansion of Eurocurrency lending to nonbank borrowers has aggravated inflation throughout the world. \* \* \*.

### International trade

The premier achievements during the 1970's in the area of trade policy were the successful avoidance of the restrictions that would have been imposed by the legislation Representative Burke and Senator Hartke sponsored at the beginning of the decade, the introduction of the generalized system of preferences to open the U.S. market to selected imports from developing countries, and the successful conclusion of the Tokyo Round of multilateral trade negotiations.

\*\*\* At no time in this century, at least, has the United States persisted in reducing tariffs and removing other obstacles to trade in the face of such massive obstacles—the sharpest and deepest recession since the Great Depression and successive multiplication of oil prices. \*\*\* Successful recycling of OPEC revenues and the relatively rapid rebound in the United States from the 1974–75 recession helped avoid the retreat into protectionism that could have overwhelmed the multilateral trade negotiations.

\*\*\* Tariffs for most industrial products have been reduced to such a low level that they are generally no longer significant obstacles to trade. Thus, there was a major shift in emphasis during this last round of negotiations toward attempts to eliminate nontariff impediments to trade. \*\*\* Without improved international agreements in these areas, competition among governments, to our mutual disadvantage, is bound to increase. \*\*\*.

The relative competitive position of the United States is likely to be a focus of concern during the next decade, for at least three reasons. First, as a consequence of rising energy prices and, hence, slow growth in the industrial world, competition for export markets is likely to intensify generally. Competition for sales to OPEC is likely to be particularly intense. Second, the advanced developing countries—Brazil, Mexico, Singapore, Hong Kong, Taiwan, and South Korea are the prime examples—made great strides in the 1970's, including adjustment to high energy costs. In the 1980's they can be expected to maintain above-average rates of productivity growth, as well as to expand further into the export of sophisticated products designed for the huge U.S. market. \*\*\* Third, the United States has relied heavily during the 1970's on relative price changes via dollar depreciation to bolster its sagging international competitive position. But the adverse consequences of dollar depreciation in terms of boosting domestic inflation and impairing Americans real incomes, both relatively and absolutely, are progressively becoming more evident.

Difficult choices face the United States, choices that our democratic processes have only begun to struggle with. Some other societies, partly as a consequence of closer cooperation than in the United States among government, industry, and labor, are manifestly out-performing this country in improving the life styles of their populations and in adjusting to traumas of international economic reality. There is widespread domestic dissatisfaction with our productivity growth relative, both to other countries and to our own performance in the 1960's. Among the pains of combating inflation by maintaining restrictive fiscal and monetary policies, in addition to unemployment, is also the negative impact on investment and productivity.

There are fears that the United States is ad hoc slipping into a policy of retrenchment when a conscious unified effort to select the evolution of our economy would produce a far more preferable outcome. \*\*\*.

\*\*\* Failure to develop more effective communication and cooperation among government, industry and labor in the 1980's would mean further impairment of the relative U.S. position. Only with general agreement on the need to bolster U.S. global economic leadership can incentives to save and invest, to generate product innovations, to shift employment into growth industries, and to export, yield maximum benefits.

### International energy policy

The external aspects of U.S. energy policy are the outgrowth of domestic decisions, even though the need to restructure domestic energy policy is the direct consequence of higher OPEC petroleum prices and reduced availability. \*\*\* The United States is making good progress, after a delayed start, towards this restructuring of our economy. Indeed, during 1979 the United States is the only one of the major industrial countries that has reduced its petroleum consumption.

### Geographical shifts in the emphasis of U.S. policy

While in no way ignoring Europe, \*\*\* during the 1970's the attention of American economic policymakers expanded to take account of Japan's emergence as the second largest market economy and to acknowledge the growing importance of the Pacific Basin more generally. It is the area of most dynamic economic growth and one to which the United States will be obliged to devote increasing attention as we move into

the eighties. Some of the Pacific advanced developing countries may even graduate to industrial status during the next decade. They, in turn, as well as Brazil and Mexico, will provide both examples and markets for the less developed countries in that group's continuing upward striving.

\* \* \* Research in Treasury indicates that participation in the multilateral development banks is not only a sound investment in future global prosperity and reduced political conflict, but participation also brings important benefits to the United States. For every dollar the U.S. contributes to the banks, our exports increase between \$2 and \$3. \* \* \*.

### **U.S. international economic leadership**

During the last decade the United States helped stabilize the world and insure an environment in which economic growth could occur by bearing major responsibilities for the mutual defense of the market economies. \* \* \*.

Following the 1973-74 oil price shock, the United States helped stabilize the global economy by encouraging commercial bank recycling of OPEC revenues and by promoting a rapid recovery from our sharp recession.

In recent years U.S. monetary authorities have moved to acquire an expanded volume of resources and use them as necessary for stabilizing exchange markets. In addition, we look to surveillance by the IMF as a major initiative in promoting macroeconomic policy coordination among the leading industrial countries.

The United States maintained and expanded the course of trade liberalization and eliminated restraints on international capital flows. \* \* \*.

To deal with high energy prices and questionable availability of petroleum in the 1980's, the United States has introduced an import quota, is freeing energy prices, and in the current year has cut petroleum consumption.

\* \* \* \* \*

In looking forward to the eighties, our main tasks are to bring inflation under control, to continue the shift to domestically produced fossil, synthetic, and renewable energy resources, and to gird the U.S. international competitive position with higher rates of savings and investment, aggressive innovation, and a willingness on the part of all aspects of American society to work together towards maintaining the economic primacy that is essential to our military and political leadership.

## **Testimony on International Matters**

### **Exhibit 80.—Other Treasury testimony in hearings before congressional committees**

#### **Secretary Miller**

Statement published in hearings before the Subcommittee on International Development Institutions and Finance of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 96th Congress, 2d session, regarding authorization requests for the multilateral development banks for 1980, March 26, 1980, pp. 21-52.

Statement published in hearings before the Subcommittee on Foreign Operations and Related Programs of the Committee on Appropriations, House of Representatives, 96th Congress, 2d session, regarding legislation providing for the maintenance of the U.S. share of the IMF quotas and the administration's FY 1981 appropriations request for the multilateral development banks, March 26, 1980, pp. 2-39.

#### **Under Secretary for Monetary Affairs Solomon**

Statement before the Subcommittee on International Finance of the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 96th Congress, 1st session, regarding the Euromarkets, international debt, the economic effects of oil price increases, and the evolution of the international monetary system, December 12, 1979.



### Assistant Secretary for International Affairs Bergsten

Statement published in hearings before the Subcommittee on Africa of the Committee on Foreign Affairs, House of Representatives, 96th Congress, 1st session, regarding U.S. economic interests and policies in Africa, October 25, 1979, pp. 249-71.

Statement published in hearings before the Subcommittee on International Finance of the Committee on Banking, Housing and Urban Affairs, U.S. Senate, 96th Congress, 2d session, regarding the first concurrent resolution for the fiscal 1981 Federal budget and on supplementals to the fiscal 1980 budget as regards the Export-Import Bank of the United States, February 22, 1980, pp. 80-89.

Statement published in hearings before the Committee on Foreign Relations, U.S. Senate, 96th Congress, 1st session, regarding authorization requests for the multilateral development banks for 1980, March 28, 1980, pp. 342-56.

Statement published in hearings before the Subcommittees on International Economic Policy and Trade and International Organizations of the Committee on Foreign Affairs, House of Representatives, 96th Congress, 2d session, regarding North/South economic relations, May 15, 1980, pp. 129-33.

Statement to be published in hearings before the Subcommittee on International Trade, Investment and Monetary Policy of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 96th Congress, 2d session, regarding the status of the international negotiations to improve the International Arrangement on Export Credits, June 12, 1980, pp. 9-21.

Statement to be published in hearings before the Subcommittee on International Trade of the Committee on Ways and Means, House of Representatives, 96th Congress, 2d session, regarding U.S. trade policy from the perspective of the Treasury Department, particularly the U.S. trade position and export finance, June 26, 1980, pp. 97-9.

### General Counsel Mundheim

Statement published in hearings before the Committee on Foreign Relations, U.S. Senate, 96th congress, 2d session, regarding S. 2141, payment of claims against the People's Republic of China, April 23, 1980, pp. 8-13.

## Organization and Procedure

### Exhibit 81.—Department of the Treasury orders relating to organization and procedure

#### No. 104-1, OCTOBER 1, 1979.—ORGANIZATION AND FUNCTIONS OF THE OFFICE OF THE ASSISTANT SECRETARY (ECONOMIC POLICY)

By virtue of the authority vested in me as Secretary of the Treasury, including authority vested in me by Reorganization Plan No. 26 of 1950, it is ordered:

1. The following are the functions of the Office of the Assistant Secretary (Economic Policy):

- a. Develops and maintains an economic research capability for the Treasury that is consistent with the Department's policy responsibilities.
- b. Provides the Secretary, the Deputy Secretary, and the Under Secretary (Monetary Affairs) with substantive advice and recommendations on the economic aspects of domestic policy actions that fall within their sphere of responsibility or interest.
- c. Conducts research in those areas of economic activity necessary to provide a continuous appraisal of the current state and future course of the U.S. economy.
- d. Analyzes and evaluates, in depth, the economic consequences of developments, and of alternative policy and legislative proposals, in a wide range of economic areas.

2. Office of the Deputy Assistant Secretary (Economic Policy):

- a. Serves as a full deputy to the Assistant Secretary in the conduct of the above functions and acts for the Assistant Secretary in that official's absence.
- b. Directs and closely supervises research efforts conducted by the Office of Financial Analysis and the Office of Special Studies.
- c. Plans, monitors, and evaluates research efforts, including establishing and achieving time and quality targets.
- d. Advises on the policy requirements for research, and on the policy implications of research results. Specific functions of subordinate offices are:

- (1) Office of Financial Analysis: Develops an overall appraisal of the current state of the economy and forecasts of Gross National Product (GNP). Provides most of the input for the Secretary's economic briefing book. Conducts briefings of Treasury officials, and participates in interagency groups working on these matters.
- (2) Office of Special Studies: Conducts in-depth economic evaluations and analyses of developments and issues that affect specific areas of the United States economy, i.e., labor, prices, social security, fiscal policy, regulatory reform and energy. The results are used for: (a) formulating Treasury positions on legislative or administrative proposals; (b) continually appraising current developments in each area; and (c) providing sector inputs to macroeconomic forecasts. Analyzes the effects on the U.S. economy (output, prices, Federal budget, and financial markets) of energy development and programs. Monitors and assesses the economic effects of changing energy technologies. Evaluates the effects of Government programs in developing new technologies, or in modifying the use of older technologies.

3. The Assistant Secretary (Economic Policy) is authorized to reassign functions, programs and associated positions and resources among the subordinate offices established above, as deemed necessary, consistent with existing administrative rules, regulations and procedures.

4. Treasury Order No. 104-1, dated March 30, 1979, is hereby superseded.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 108-1, OCTOBER 1, 1979.—ORGANIZATION AND RESPONSIBILITIES OF  
THE OFFICE OF THE ASSISTANT SECRETARY (INTERNATIONAL AFFAIRS)

By virtue of the authority vested in the Secretary of the Treasury, including the authority vested in me by Reorganization Plan No. 26 of 1950, it is ordered that:

1. The Assistant Secretary (International Affairs) is the principal advisor to the Secretary of the Treasury and the Under Secretary (Monetary Affairs) in exercising policy direction and control over Treasury positions in areas dealing with international financial, economic, monetary, trade, and commercial matters as well as energy policies and programs.

2. Within the Office of the Assistant Secretary (International Affairs) (OASIA), there are five Deputy Assistant Secretaries: Developing Nations, International Monetary Affairs, Trade and Investment Policy, Commodities and Natural Resources, and International Economic Analysis. The functions and responsibilities of the Deputy Assistant Secretaries are defined by the Assistant Secretary and the Deputy Assistant Secretaries serve under the policy guidance of the Assistant Secretary. Each Deputy Assistant Secretary supervises a number of offices managed by Directors. The functions and responsibilities of the Deputy Assistant Secretaries shall include, but not be limited to, the following:

- a. Deputy Assistant Secretary (Developing Nations)

- (1) The Office serves as the principal policy advisor to the Assistant Secretary in formulating and implementing Treasury positions on U.S. economic and financial programs with respect to developing nations. The Office helps initiate, review, and oversee U.S. policies toward the less developed nations on such issues as debt owed to private and public sector entities, foreign assistance, food, popula-

tion and financial policies, and evaluate the development and financial impact on the less developed nations of U.S. policies on trade, investment and commodities. Staff support is provided to senior Treasury officials in the formulation of U.S. policies on developed/developing nations relations generally, especially in connection with multilateral fora such as the UN General Assembly, UN Conference on Trade and Development (UNCTAD) and the IBRD/IMF Development Committee and its subordinate bodies. The Office maintains representatives in key developing nations who are responsible for analyzing local economic conditions and recommending appropriate policies. It also maintains liaison with and reviews policies of other USG agencies on development issues.

- (2) The Office provides comprehensive analyses and forecasts of the economic, financial, and political situation in developing countries for use in formulating Treasury policy on financial assistance, debt rescheduling, and other matters. The Office collects and maintains data on all LDCs including the OPEC countries, giving particular attention to balance of payments, official and private capital flows, debt and IMF credit. The Office also has the responsibility for providing support to the Secretary of the Treasury as a member of the joint economic commissions which have been established with individual developing countries, other than Saudi Arabia.
- (3) The Office formulates, reviews, and oversees Treasury positions on policies, operations, and activities of the international lending institutions and the activities of the International Monetary Fund related to developing nations. The Office maintains liaison with and reviews policies of international, United States, and interagency development finance and policy formulating bodies, such as the Development Assistance Committee of the OECD and the Development Loan Staff Committee. The Office administers the Secretariat of the National Advisory Council on International Monetary and Financial Policies (NAC). The NAC operates under the authority of Executive Order No. 11269.

b. Deputy Assistant Secretary (International Monetary Affairs)

- (1) The Office serves as the principal policy advisor to the Assistant Secretary in formulating and implementing Treasury policies concerned with (a) the maintenance and operation of a smoothly functioning international monetary system, including the role of the private money and capital markets; (b) coordination of economic policy among industrial nations; (c) the development and conduct of U.S. financial relations with the market economy industrial nations; (d) monetary relationships with the U.S. Government sought by other nations; (e) foreign exchange operations and management of U.S. reserve assets; (f) international borrowing, portfolio investment and insurance. In carrying out these functions the Office provides support for U.S. participation in multilateral financial institutions, principally the International Monetary Fund and the OECD, as well as in other fora related to its functional areas of responsibility.
- (2) The Office provides analyses and forecasts of economic developments in and policies of the major industrial nations, both domestic and external. It maintains Treasury representatives in key industrial countries and in the OECD. It also analyzes and forecasts regional and global payments patterns and their implications for the functioning of the monetary system.
- (3) With guidance furnished by senior Treasury officials, direction is given to the Federal Reserve Bank of New York concerning ESF operations and liaison is maintained to assure that foreign operations of the Federal Reserve System are coordinated. In this regard, foreign exchange markets are intensively monitored. Continuing



oversight of gold markets and related developments is also maintained.

- (4) The Office provides analyses and assembles information relevant to international banking, portfolio investment and insurance matters and the international practices of U.S. and foreign banks, their regulatory authorities and the impact of their activities on the operation of the international monetary system.

c. Deputy Assistant Secretary (Trade and Investment Policy)

- (1) The Office serves as the principal policy advisor to the Assistant Secretary in the areas of trade policy, trade with nonmarket economy countries, and international investment.
- (2) The Office formulates and implements Treasury positions on: (a) U.S. trade and commercial policy in general; (b) multilateral and bilateral trade negotiations; (c) trade finance matters; (d) U.S. military sales abroad; (e) U.S. economic relationships with the U.S.S.R., Eastern Europe, China, and such other nonmarket economy countries as may be designated, including support for operations of the East-West Foreign Trade Board and its Working Group; (f) programs in relation to the Secretary's responsibilities for trade relations with other countries; (g) direct investment issues, including matters pertaining to multinational corporations, expropriation and the Overseas Private Investment Corporation; and (h) serves as Secretariat for the interagency Committee on Foreign Investment in the United States established by Executive Order No. 11858.

d. Deputy Assistant Secretary (Commodities and Natural Resources)

- (1) The Office serves as the principal policy advisor to the Assistant Secretary in formulating and implementing Treasury policy and positions on questions relating to (a) international energy policy, with special emphasis on the economic, financial and investment aspects of such policy; (b) other basic natural resources, particularly non-fuel minerals and agricultural commodities; (c) U.S. commodity policy; and (d) oceans policy matters, including "Law of the Sea" negotiations.
- (2) In carrying out these functions, the Office (a) assembles information and provides analyses relevant to the formulation of commodity and international energy policies; (b) advises the Assistant Secretary and senior Treasury officials on economic and financial implications of natural resource and international energy issues which may be considered at interagency or international levels; (c) develops and implements Treasury policy with respect to natural resource issues arising in international fora, such as the International Energy Agency, the United Nations Conference on Trade and Development, the Development Committee of the International Monetary Fund and the International Bank for Reconstruction and Development (IMF/IBRD) and various committees of the Organization for Economic Cooperation and Development (OECD).

e. Deputy Assistant Secretary (International Economic Analysis)

- (1) Provides macroeconomic analyses that relate to the formulation of international economic policies. This includes analyses of the long-term effects of policies, both U.S. and foreign, on foreign trade, services and capital flows.
- (2) Prepares analyses and reports on current developments and near-term prospects for the U.S. current-account balance and for capital flows, to be utilized in forecasts of the U.S. economy and in formulation of U.S. international monetary policy.
- (3) Develops analytic techniques for anticipating problems and evaluating possible solutions, i.e., industries that are likely to need trade adjustment assistance and possible causes of monetary disturbances.

- (4) Develops analytic techniques for the study of current international economic issues, such as technological transfer and U.S. financing of Eastern Block requirements.
  - (5) Compiles and prepares for publication statistics on U.S. capital flows as required by law or traditional practice and on actual indebtedness to the U.S. Government, as well as potential liabilities under guarantee and insurance programs.
  - (6) Regularly uses commercially available and in-house macroeconomic models as tools to analyze the above; for example, the international transmission of growth and inflation, international liquidity issues, determinants of international trade and capital flows, and exchange rate changes. Provides data processing, programming, and econometric modeling assistance to other offices in OASIA.
3. Within the Office of the Assistant Secretary (International Affairs), there also are the Office of the Deputy to the Assistant Secretary (Saudi Arabian Affairs), the Deputy to the Assistant Secretary and the Secretary of the International Monetary Group, the Office of the Inspector General, the Administrative Staff, and the OASIA Secretariat. The functions and responsibilities of these offices, which are defined by the Assistant Secretary, are:
- a. The Office of the Deputy to the Assistant Secretary (Saudi Arabian Affairs) is composed of an Office of Saudi Arabian Affairs in Washington and an Office of the U.S. Representation to the Joint Commission in Riyadh, Saudi Arabia, and serves as the principal policy advisor to the Assistant Secretary in formulating and implementing the projects and programs undertaken by the U.S.-Saudi Arabian Joint Commission on Economic Cooperation established on June 8, 1974, and chaired by the Secretary of the Treasury. The Office is also responsible for the development of Treasury policy with respect to U.S. economic relations with Saudi Arabia.
  - b. The Deputy to the Assistant Secretary and Secretary of the International Monetary Group serves as a policy advisor to the Assistant Secretary in the formulation and implementation of policies relating to the international monetary system. In this connection the incumbent serves as Executive Secretary of the International Monetary Group, an interagency body chaired by the Under Secretary for Monetary Affairs, which consults with the Under Secretary on substantive matters and on negotiating positions; in this capacity, he or she provides documentation to the Group for both briefing and current updating purposes.
  - c. The Office of the Inspector General provides the Assistant Secretary and other senior level Treasury officials with a reliable and independent internal appraisal of selected international financial activities and programs for which OASIA has primary operational responsibility. The Inspector General also performs such reviews as requested. Major areas of concern include the efficiency and economy of the use of U.S. investments in the International Monetary Fund, the International Bank for Reconstruction and Development, and regional multilateral banks, as well as procedures governing the use of the ESF.
  - d. The Administrative Staff and OASIA Secretariat perform administrative and other support operations for the Assistant Secretary.
4. With the exception of the Office of the Inspector General, the Assistant Secretary may reassign programs, functions, and associated positions and resources among the subordinate offices established above as deemed necessary, consistent with the policies and procedures governing the ESF.

5. This Order supersedes Treasury Order No. 202 (Rev. 3), dated August 25, 1977.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 101-12, OCTOBER 12, 1979.—DELEGATION OF AUTHORITY TO THE  
OFFICE OF ADMINISTRATIVE PROGRAMS AND TREASURY BUREAUS TO AFFIX  
THE SEAL OF THE DEPARTMENT OF THE TREASURY

By virtue of the authority vested in the Secretary of the Treasury including the authority conferred by 5 U.S.C. 301, and by virtue of the authority delegated to me by Treasury Order No. 101-5, it is hereby ordered that Heads of Bureaus and their deputies are authorized to affix the Seal of the Department of the Treasury in authentication of originals and copies of books, records, papers, writings, and documents of the Department, for all purposes, including the purposes authorized by 28 U.S.C. 1733(b).

Heads of Bureaus or their deputies may delegate this authority to appropriate subordinate officials.

In the Office of the Secretary, the following are authorized to affix the Seal of the Department of the Treasury:

Director, Office of Administrative Programs  
Deputy Director, Office of Administrative Programs  
Manager, Facilities Services Division  
Chief, Communications and Records Management Branch  
Chief, Reference and Distribution Section

Heads of Bureaus and the Director, Office of Administrative Programs are authorized to procure and maintain custody of the dies of the Treasury Seal.

This Order supersedes Treasury Department Order No. 107 (Revision 20) dated December 21, 1976.

W. J. McDONALD,  
*Assistant Secretary (Administration).*

NO. 101-3, FEBRUARY 20, 1980.—DELEGATION OF PROCUREMENT  
AUTHORITY TO OFFICE OF PROCUREMENT AND TREASURY BUREAUS

By virtue of the authority vested in me as Assistant Secretary (Administration) by Treasury Department Order No. 208, Revision 4, it is ordered:

1. The Director, Office of Procurement, Office of the Secretary, is delegated the authority to prescribe and publish Treasury Procurement Regulations. This authority may not be redelegated.

2. The following officials of the Department of the Treasury are delegated the authority to procure property and services consistent with Title III of the Federal Property and Administrative Services Act of 1949 (Act), as amended (41 USC 251-260), except as precluded by Section 307 (41 USC 257) of the Act:

Director, Office of Procurement, Office of the Secretary  
Director, Bureau of Alcohol, Tobacco and Firearms  
Comptroller of the Currency  
Commissioner of Customs  
Director, Bureau of Engraving and Printing  
Director, Federal Law Enforcement Training Center  
Commissioner, Bureau of Government Financial Operations  
Commissioner of Internal Revenue  
Director of the Mint  
Commissioner of the Public Debt  
National Director, U.S. Savings Bonds Division  
Director, U.S. Secret Service

3. Each of the officials named in paragraph 2 is deemed "chief officer responsible for procurement" within the meaning of 41 USC 257 (b).



4. The authority delegated includes but is not limited to:
  - a. entering into and taking all necessary actions with respect to purchases, contracts, leases, and other contractual procurement transactions;
  - b. making determinations and decisions with respect to procurement matters, except those determinations and decisions required by law or regulation to be made by other authority; and
  - c. designating persons qualified in procurement matters as Contracting Officers and representatives thereof, in accordance with requirements and procedures established in Section 1.404 of the "Treasury Procurement Regulations."

5. The authority delegated shall be exercised in accordance with the applicable limitations and requirements of the Act; the Federal Procurement Regulations, 41 CFR Chap. 1; the applicable portions of the Federal Property Management Regulations, 41 CFR Chap. 101; as well as regulations issued by the Department of the Treasury which implement and supplement the Federal Procurement Regulations and the Federal Property Management Regulations including but not limited to 41 CFR Chap. 10 and Treasury Directives Manual Chapter 70-06, "Treasury Procurement Regulations."

6. To the extent permitted by the Act and this delegation, the authority delegated to the above-named officials may be redelegated by them by letter or bureau order to any subordinate officer or employee of their respective organizations who has been duly designated to act as a Contracting Officer for the United States.

This Order supersedes Department of the Treasury Order 101-3, dated July 16, 1979.

W. J. McDONALD,  
*Assistant Secretary (Administration).*

#### NO. 101-14, FEBRUARY 20, 1980.—TRANSFER OF THE OFFICE OF AUDIT TO THE INSPECTOR GENERAL

Pursuant to the authority vested in me as Secretary of the Treasury, including the authority contained in Reorganization Plan No. 26 of 1950, it is ordered that:

1. The Office of Audit is transferred from the jurisdiction and supervision of the Assistant Secretary (Administration) to that of the Inspector General; specifically transferred are the personnel, records, property, duties, and responsibilities of the Office of Audit except the following responsibilities and associated resources which shall be retained by the Assistant Secretary (Administration):

- a. Accounting Policy. The responsibilities for providing professional assistance to Treasury bureaus on improving financial management as it relates to administrative appropriations. This includes the review and appraisal of accounting systems in operation and the approval of new or modified systems preparatory to obtaining final approval by the Comptroller General of the United States.
- b. Travel Policy. The responsibilities for developing and interpreting Treasury travel policies consistent with GSA and other Government regulations and reviewing, on behalf of the Deputy Secretary, bureau requests for use of first class travel.

2. This Order is effective immediately.

3. This Order supersedes Treasury Department Order No. 200 (Amendment 1) dated June 24, 1971.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

#### NO. 102-6, FEBRUARY 20, 1980.—ESTABLISHMENT OF THE OFFICE OF PROCUREMENT

By virtue of the authority vested in the Secretary of the Treasury by Reorganization Plan No. 26 of 1950, and pursuant to the authority delegated to me by Treasury Order No. 101-5:

1. The Office of Procurement is established under the direct supervision of the Assistant Secretary (Administration).
2. Personnel, records, property, duties and responsibilities of the Assistant Director (Procurement) are transferred from the Office of Administrative Programs to the Office of Procurement.

W. J. McDONALD,  
*Assistant Secretary (Administration).*

NO. 101-15, FEBRUARY 27, 1980.—DELEGATIONS OF AUTHORITY TO THE  
DEPUTY SECRETARY AND INSPECTOR GENERAL RELATING TO TREASURY  
AUDITING AND INSPECTION ACTIVITIES

By virtue of the authority vested in me as Secretary of the Treasury, including the authority contained in Reorganization Plan No. 26 of 1950, it is ordered that:

1. The Deputy Secretary shall be, any other Treasury delegation notwithstanding, the appointing authority authorized to take all final personnel action with respect to the positions listed in 2 below.
  - a. Heads of Bureaus shall screen and recommend candidates for vacancies to the Deputy Secretary. The Inspector General shall be consulted by the bureaus throughout the recruitment and selection process. The recommendations to fill the vacancies shall be submitted to the Deputy Secretary through the Inspector General.
  - b. Heads of Bureaus shall evaluate, in accordance with normal procedures, the performance of the incumbents of the positions and submit the performance evaluations to the Deputy Secretary through the Inspector General.
2. The Inspection and Audit positions, listed below, shall, in addition to their present reporting responsibilities, report directly to the Inspector General.

Assistant Commissioner (Inspection), Internal Revenue Service  
Assistant Commissioner (Management Integrity), U.S. Customs Service  
Assistant Director (Internal Affairs), Bureau of Alcohol, Tobacco and  
Firearms

Assistant Director (Inspection), U.S. Secret Service  
Chief, Office of Audit and Internal Affairs, Bureau of Engraving and  
Printing

Director, Inspection and Audits, Comptroller of the Currency  
Assistant Commissioner, Comptroller, Bureau of Government Financial  
Operations

Director, Division of Internal Audit, Bureau of the Public Debt (and  
Savings Bonds)

Chief, Internal Audit Staff, Bureau of the Mint

Chief, Internal Audit Staff, Federal Law Enforcement Training Center

3. The Inspector General shall exercise the following additional authority:
  - a. review and approve bureau and office audit and inspection programs and plans;
  - b. evaluate bureau and office audit and inspection programs; and
  - c. require, receive, review, and analyze reports informing the Secretary or Deputy Secretary of any significant problems, abuses, or deficiencies disclosed in bureau audits and investigations and the actions taken to correct them.
4. The Inspector General shall promulgate rules, regulations, orders, and directives to carry out the responsibilities assigned to the Inspector General by this Order.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 101-16, MARCH 1, 1980.—CHANGE IN SUPERVISION OF THE FISCAL  
ASSISTANT SECRETARY

Pursuant to the authority vested in me by Reorganization Plan No. 26 of 1950, it is ordered that:

1. The Fiscal Assistant Secretary shall be under the supervision of the Under Secretary, and shall exercise supervision over the Commissioner, Bureau of Government Financial Operations, and the Commissioner of the Public Debt.

2. This Order is effective immediately.

3. Treasury Order No. 101-5 will be updated accordingly.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 101-17, MARCH 1, 1980.—CHANGE IN SUPERVISION OF THE ASSISTANT SECRETARY (DOMESTIC FINANCE)

Pursuant to the authority vested in me by Reorganization Plan No. 26 of 1950, it is ordered that:

1. The Assistant Secretary (Domestic Finance) shall be under the supervision of the Secretary, and shall report to the Secretary through the Deputy Secretary, including reporting for debt management purposes.

2. This Order is effective immediately.

3. Treasury Order No. 101-5 will be updated accordingly.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 102-4, JUNE 12, 1980.—ORGANIZATIONAL STRUCTURE, OFFICE OF THE ASSISTANT SECRETARY (ADMINISTRATION)

By virtue of the authority vested in the Secretary of the Treasury by Reorganization Plan No. 26 of 1950, and pursuant to the authority delegated to me by Treasury Order No. 101-5, the following is the organizational structure within the Office of the Assistant Secretary (Administration):

1. Office of Administrative Programs. Directs Department-wide programs relating to emergency preparedness, energy conservation, environmental programs, the Freedom of Information and Privacy Acts, historic preservation, physical security, printing management, safety and occupational health, real and personal property management, and telecommunications management. Administers Department-wide voluntary action programs and develops related policies and procedures for carrying out these programs. Manages Departmental library services and printing facilities. Provides facilities management services to the Office of the Secretary, including administrative travel support; audiovisual services; communications and records management; security operations; and space and property management.

2. Office of Budget and Program Analysis. Prepares, presents, and justifies estimates of the Department's appropriations and plans. Maintains liaison with other agencies, central Government staff agencies and Congress and represents the Department in dealing with those organizations concerning analysis of activities and programs, and concerning budgetary matters. Also, is responsible for accounting policy and travel policy for the Department.

3. Office of Computer Science. Furnishes computer and related support for the analytical, policy formulation, accounting, and administrative functions of the Office of the Secretary and the bureaus. Assists in computer development work for bureaus which do not have their own computer facilities. Provides Department-wide, centralized management review, approval, and guidance for ADP management planning, policy, and evaluation activities.

4. Office of Equal Opportunity Program. Directs Treasury's Equal Employment Opportunity Program, establishing policies, plans, and procedures. Administers the Federal Women's Program and Hispanic Employment Program. Also administers Treasury's discrimination complaint system.

5. Office of Management and Organization. Performs its specific functions through the following organizational elements:

a. Office of the Assistant Director (Financial Management). Provides budget and accounting services for the ten different appropriations and/or accounts that make up the financial structure of the Office of the Secretary. This includes



- budget formulation, justification, execution and liaison with OMB and Congressional staffs. The accounting branch provides the full range of accounting services including systems and payroll interface with the Departmental system.
- b. Office of the Assistant Director (Management Analysis). Directs the Department's management improvement, productivity management, information resources management, A-76, international visitors, advisory committee and ZBBO programs; advises and assists officials on matters of management and organization and information resources management; conducts studies of organizations, management systems and programs; and supports the Assistant Secretary (Administration) in the development and coordination of various special programs.
  - c. Office of the Assistant Director (Personnel Management). Administers the personnel management program within the Office of the Secretary. Formulates personnel policies and programs, and establishes procedures to implement Office of Personnel Management and Departmental personnel policies.
  - d. Office of the Assistant Director (Treasury Payroll/Personnel Information Systems). Provides automated payroll/personnel information systems services to each of the Department's bureaus (except IRS) including the fulfillment of Department-wide personnel, payroll, report, and control requirements. Establishes, maintains, and refines the Departmental payroll and personnel information system and its interface with related systems. Manages and operates a system of procedures and computer programs designed to fulfill these Department-wide requirements.
  6. Office of Personnel. Develops policy and procedures and implements personnel programs and personnel management evaluation systems relating to executive resource management, Civil Service Reform Act implementation, recruitment, appointment, promotion, classification, pay, fringe benefits, health, training, career development, recognition, labor-management relations, security clearances, and appeals of employees and positions throughout the Department of the Treasury.
  7. Office of Procurement. Provides policy and technical guidance for the Department's procurement and contracting programs. Conducts evaluations of bureau procurement operations. Effects centralized procurement of items used by several bureaus where feasible. Conducts operational procurement support for Office of the Secretary organizations and for the Saudi Arabian Government under the Technical Cooperation Agreement with that country.
  8. Office of the Secretary Equal Employment Opportunity Staff. Administers the Equal Employment Opportunity Program, including the Federal Women's Program and Hispanic Employment Program, within the Office of the Secretary. Also administers Treasury's discrimination complaint system within the Office of the Secretary.
  9. This Order supersedes Treasury Order 102-4 dated February 29, 1980.

W. J. McDONALD,  
*Assistant Secretary (Administration).*

**NO. 101-18, JUNE 13, 1980.—DELEGATION OF AUTHORITY TO BUREAUS TO  
ADVISE ON QUESTIONABLE PAYMENTS OF \$25 OR LESS**

By virtue of the authority vested in the Secretary of the Treasury by Reorganization Plan No. 26 of 1950; the Comptroller General's letter, B-161457, "Payments of \$25 or Less" dated July 14, 1976; and pursuant to the authority delegated to me by Treasury Department Order No. 101-5, it is hereby ordered (1) that the Heads of Bureaus in the Department are delegated the authority to appoint a bureau official to whom disbursing and certifying officers may apply for and obtain advice on questions involving payments of \$25 or less, and (2) that the General Counsel, or his/her delegate, shall be the appointed official in the Office of the Secretary.

Under existing law, disbursing officers and certifying officers may apply for and obtain a decision from the Comptroller General of the United States on any question involving a payment to be made by them or a payment on any voucher presented for certification (31 U.S.C. 74, *id.* 82d). After this order is implemented, the General Accounting Office (GAO) will rely on each of the delegated bureau official's advice

involving questionable minor amounts of \$25 or less. A copy of the document containing such advice should be attached to the voucher and will be considered conclusive by GAO in its settlement of the accounts involved.

W. J. McDONALD,  
*Assistant Secretary (Administration).*

NO. 106-2, JUNE 25, 1980.—DELEGATION OF AUTHORITY TO THE FISCAL ASSISTANT SECRETARY TO CARRY OUT ADMINISTRATION AND ACCOUNTING FOR SALES OF GOLD MEDALLIONS

By virtue of the authority vested in me as Secretary of the Treasury, including the authority of the American Arts Gold Medallion Act and Reorganization Plan No. 26 of 1950, it is ordered:

1. The Fiscal Assistant Secretary is hereby authorized:
  - a. To take all necessary and proper measures for the administration and accounting for sales of American Arts Gold Medallions, under the general policy supervision of the Deputy Secretary.
  - b. After each sale of gold medallions by the Department of the Treasury, or other Federal agencies under the policy direction of the Department of the Treasury, to take all necessary and proper steps in cooperation with those other Federal Agencies under the policy direction of the Treasury and/or other Bureaus of the Treasury, to arrange for the transfer of any gold purchased and to account for all receipts and disbursements in connection with the sale of the gold medallions.
  - c. To arrange for redemption of gold certificates held by the Federal Reserve System.
2. The Fiscal Assistant Secretary may redelegate this authority to other officials of the Treasury, including the Director of the Mint and Commissioner, Bureau of Government Financial Operations. Any actions heretofore taken by the Fiscal Assistant Secretary to arrange for administration and accounting for the aforementioned sales are hereby ratified and confirmed.

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

NO. 103-1, SEPTEMBER 15, 1980.—ORGANIZATION AND FUNCTIONS OF THE OFFICE OF THE ASSISTANT SECRETARY (DOMESTIC FINANCE)

By virtue of the authority vested in me as the Secretary of the Treasury, including the authority of the Reorganization Plan No. 26 of 1950, the following revisions and additions to the Office of the Assistant Secretary (Domestic Finance) organizational structure are hereby ordered to be effective immediately:

1. The following are the functions of the Office of the Assistant Secretary (Domestic Finance):
  - a. Advises and assists the Secretary and Deputy Secretary of the Treasury, and the Under Secretary for Monetary Affairs, on debt management, Federal financing affairs, financing of non-Federal sectors of the economy, and general capital markets policy.
  - b. Directs the Treasury operations that relate to: (1) the Federal Financing Bank; (2) the development of legislative and administrative principles and standards for Federal credit programs; and (3) the determinations of interest rates for various Federal borrowing, lending, and investment purposes under pertinent statutes.
  - c. Administers Treasury operations under the New York City Loan Guarantee Act of 1978 (PL 95-339), as well as the formation of Treasury policy dealing with general problems of State and local finance and urban economics.
  - d. Administers Treasury operations under the Chrysler Corporation Loan Guarantee Act of 1979 (PL 96-185).
  - e. Also, exercises policy direction and control over Treasury staff work on the substance of proposed legislation relating to the general activities and

regulation of private financial intermediaries, and coordinates Treasury activities relating to financing regulatory agencies.

2. The Office of the Deputy Assistant Secretary (Debt Management) is renamed the Office of the Deputy Assistant Secretary (Federal Finance). Within this office are the following:

- a. The Office of Government Financing which provides the Assistant Secretary (Domestic Finance) with technical assistance, financial and economic data, and background briefing on matters related to government financing and public debt management.
- b. The Office of Market Analysis and Agency Finance which provides for: (1) an on-going review of Federal credit programs; (2) approving and coordinating the borrowings of Federal and federally-sponsored agencies, and federally guaranteed entities; (3) monitoring the volume of funds raised and supplied in the credit markets and preparing flow-of-funds projections; (4) determining interest rates to be used in loan programs throughout the government; and (5) administering the operation of the Federal Financing Bank.
- c. The Office of the Senior Advisor (Debt Research) is abolished and the responsibilities and duties of this office are transferred to the Office of Market Analysis and Agency Finance.

3. The Office of the Deputy Assistant Secretary (Capital Markets Policy) is renamed the Office of the Deputy Assistant Secretary (Financial Institutions and Capital Markets Policy). Within this office are the following:

- a. The Office of Capital Markets Legislation which coordinates the Treasury Department's legislative effort with regard to financial institutions legislation and legislation affecting the agencies of the Federal government that regulate financial institutions.
- b. The Office of Securities Markets Policy which develops the Treasury Department's policy on all matters relating to the rules and regulations of, and the investigations conducted by, the Securities and Exchange Commission.

4. The Office of the Deputy to the Assistant Secretary (Corporate Finance) is established to provide for the following:

- a. The Office of Corporate Finance and Special Projects which provides a focal point for the comprehensive analysis of the Federal government's involvement in financing in the corporate sector of the economy.

5. The Office of Chrysler Finance is established to provide support to the Chrysler Loan Guarantee Board and the Secretary of the Treasury in his role as Chairman of that Board on matters relating to the Chrysler Loan Guarantee Act of 1979 (PL 96-185).

6. The Office of the Deputy Assistant Secretary for Urban Finance is renamed the Office of the Deputy Assistant Secretary (State & Local Finance). Within this office are the following:

- a. The Office of Municipal Finance which monitors, evaluates, and analyzes the impact of fiscal and financial conditions relating to the financial management policies and practices of State and local governments, and the municipal credit market.
- b. The Office of Urban Economics is renamed the Office of Urban and Regional Economics. The office monitors and evaluates State and local financial trends, particularly as they affect, or are affected by, Federal fiscal and grant-in-aid policies.
- c. The Office of State and Local Fiscal Research and Evaluation is established to provide evaluations of the effects on State and local financial and economic conditions and practices of all existing Federal programs, pending legislation, and tax or regulatory proposals.
- d. The Office of New York Finance carries out the obligations under the New York City Loan Guarantee Act of 1978 (PL 95-339).

7. The Office of Revenue Sharing shall administer the operations and responsibilities of the Treasury Department under the State and Local Fiscal Assistance Act of 1972 (PL 95-512), amended 1976 by (PL 94-488). The Office of Revenue Sharing shall coordinate, on matters relating to policy, with the Deputy Assistant Secretary (State &



Local Finance) but shall continue to report to the Assistant Secretary (Domestic Finance).

This order supersedes the following Treasury Department Orders: No. 242-1 (dated May 11, 1976); No. 242 (Revision 1) (dated May 17, 1977); No. 170-5 (dated September 26, 1957); No. 170-14 (dated June 11, 1973); No. 224 (dated January 26, 1973); and No. 243 (dated August 27, 1976).

G. WILLIAM MILLER,  
*Secretary of the Treasury.*

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